



CAPITALIZING ON TRUST

Harnessing Somali Remittances for Counterterrorism, Human Rights and State Building

BY JAMES COCKAYNE WITH LIAT SHETRET

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Somali Americans rally at the Minnesota State Capitol to protest the closure of money service businesses Friday, Jan. 6, 2012, in St. Paul, Minn. They are asking banks to restore relations with the companies wiring money to millions of Somali refugees in the Horn of Africa.

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About the Center on Global Counterterrorism Cooperation

THE CENTER ON GLOBAL COUNTERTERRORISM COOPERATION is a nonpartisan, nonprofit research institute. We work with governments, civil society, the private sector, the United Nations, and regional organizations to strengthen partnerships against terrorism. See www.globalct.org.

Research Team

TEAM LEADER AND AUTHOR

JAMES COCKAYNE is Co-Director of the Center and leads its work on East Africa. Trained as a lawyer, James' research focuses on international responses to transnational threats. His books include *Peace Operations and Organized Crime: Enemies or Allies?* (coedited with Adam Lupel) (2011) and *Beyond Market Forces: Regulating the Global Security Industry* (2009). He was previously a senior fellow at the International Peace Institute; chair of the Editorial Committee of the *Journal of International Criminal Justice*; an editorial committee member of the *Journal of International Humanitarian Legal Studies*; principal legal officer in the Transnational Crime Unit of the Australian Attorney-General's Department. He also worked in war crimes trials in Sierra Leone and Tanzania.

COAUTHOR

LIAT SHETRET is a Programs Officer at the Center. Liat developed the regulator questionnaire and conducted interviews with Somali remittance organizations in Dubai. She contributed substantially to the background research for this report and assisted with its drafting. She has expertise in terrorism, counterterrorism, and violent radicalization issues and political psychology, as well as Middle Eastern, East African, and Horn of Africa affairs. Liat previously served as the Harold Rosenthal Fellow in International Affairs to the U.S. House of Representatives Committee on Homeland Security. She holds a BA in political science and psychology from the University of Illinois and a Master of International Affairs degree from Columbia University's School of International and Public Affairs.

RESEARCH ASSISTANT

JOSHUA WEAVER is a researcher based in Goshen, Indiana, who served as a research consultant to the project during the literature review. He is a graduate of Associated Mennonite Biblical Seminary where he earned an MA in theological studies, with a concentration in theology and ethics.

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Glossary and Acronyms

agent An individual who receives value from a remittance sender and/or distributes payment to the recipient

AML Anti-money laundering

bah The principal domestic unit, traditionally consisting of uterine siblings

CFT Countering the financing of terrorism

clan Strong lineage-based social units that provide the principal source of identity and security in Somali society

corridor A particular route, whether physical or virtual, along which remittances habitually flow

diya Clan-based compensation payment; also called *mag*

FATF Financial Action Task Force

FERG Foreign Exchange and Remittance Group (UAE)

FIU Financial intelligence unit

franco valuta A process of remitting wealth and importing goods prominent in Somalia in the 1970s and 1980s, which relies on a person importing goods based on a foreign currency account abroad without foreign exchange expenditures from the local bank

FSA Financial Services Authority

hagbad A group engaged in collecting funds conventionally from personal savings, relatives, contributions, or microfinance organizations, often led by women, and also known as *shalongo* or *ayuuuto*

HMRC Her Majesty's Revenue and Customs (UK)

jilib The *diya* paying unit and the basic political and jural unit of Somali society

KYC Know your customer

OECD Organisation for Economic Co-operation and Development

passporting Process by which financial institutions licensed in one jurisdiction are allowed to operate across a number of jurisdictions

PEP Politically Exposed Person

bank wire stream Ongoing flow of nontrade financial transactions such as personal remittances, used in this report to connote the movement of remittances from OECD countries via formal bank wire channels to a trade hub (e.g., Dubai or Eastleigh, Nairobi); see also "trade stream."

SAR Suspicious activity report

SFSA Somali Financial Services Association

SOMTA Somali Money Transfer Association

SRO Somali remittance organization, which is run by Somalis or operates in Somalia or Somali communities and conducts nonbank financial transfers involving cash payments at one end of the transaction

STR Suspicious transaction report

TFG Transitional Federal Government of Somalia

trade stream Ongoing flow of trade finance transactions as a method of transferring value from one area to another, used in this report to connote the movement of remittance value from a trade hub (e.g., Dubai or Eastleigh) to the final recipient

UKMTA UK Money Transmitters Association

UNDP UN Development Programme

xawilaad Money transfer enterprises (in Somali), also commonly known as *hawala*

xeer Somali political and social contract

zakat Islamic duty to provide charitable donations to the poor

Executive Summary

Somalia is struggling with war, drought, and terrorism. Yet the Somali diaspora community offers a lifeline, with some \$1.0–1.5 billion being remitted each year. How to ensure these remittances support an end to war and drought rather than support terrorism? This report offers new analysis of the Somali remittance industry and ideas for improving its regulation, including combating money laundering and countering terrorist financing.

Trust is central to this industry’s business model, and we argue trust is the key to improving its regulation. This report, generously supported by the Royal Government of Denmark, draws on six months’ desk research; 27 interviews with Somali remittance organizations (SROs) working in East Africa, the Middle East, Europe, and North America; and interviews and a survey of regulators in those same regions. It explores what we know about how Somali remittances are organized, how they are regulated, and how we might strengthen that regulation in a way that underwrites Somali peace, prosperity, and human rights in the short and long term.

PUTTING SOMALI REMITTANCES IN CONTEXT

The **first part** of this report provides a brief overview of how SROs are organized. They offer a traditional system in a modernized setting, an alternative to Western formal banking in an economy that operates without formal state regulation. It is a system powered by trust.

The collapse of the Somali state in the 1990s led to a general economic breakdown of the formal banking infrastructure. In its place, Somali entrepreneurship and savvy business practices have filled the void left behind. This has led to a bustling local economy that uses remittance channels not only for family income support, but also as a vehicle for commercial trade financing, tying Somalia’s economy closely to financial and trading hubs in Kenya and the United Arab Emirates.

Our analysis suggests that Somali remittance practices have their roots in traditional aspects of Somali social and political organization, including traditional systems of collective financial support and social insurance. Somali society is historically nomadic, with “nuclear” family units (parents and children) often spending sustained periods dispersed between rural and urban communities, intermixed with other nuclear family units from the same clan or lineage group. The circulation of assets and value within these distributed networks was not necessarily considered a discrete market-based transaction (a donation, a loan, or an investment) as it might be in more modernized societies. Instead, value is frequently circulated within these social groups as part of a larger social and, in some senses, financial contract. Somali clans are traditionally subdivided into subclans, primary lineages, and clan-based compensation (*diya*) payment groups. These *jilib* groups are the most stable and important political and social unit. Members of a *jilib* are bound by shared obligations of common defense, payment of blood compensation, and mutual financial and material aid. There is thus a long-standing Somali tradition of trust-based financial transfers over large distances through family networks. Today, Somali remittances still play a similar role in modernized settings.

Diaspora members sending money home are frequently fulfilling a social duty and familial obligation, supporting family members and, increasingly, members of other clans through famine, war, and drought. Somalis regularly send money home to brothers, sisters, children, spouses, parents, and grandparents living in economic hardship. Somalis who think about eventually returning to the homeland may also send back money to invest in a future home, a construction project, or a relative’s education. What is particularly extraordinary about this system is just how frequently Somalis remit relatively significant amounts of money despite their comparative poverty in global terms.

We find that Somalis living abroad collectively send around \$1.0–1.5 billion annually through SROs, ranking Somalia’s economy among the most heavily remittance dependent in the world. The financial coverage of SROs is extensive; some claim that SRO networks cover nearly the whole country. Remittances are resilient, withstanding social crises such as war, famine, and tsunamis. SROs are also an important source of employment and income within Somalia and within the Somali diaspora. Remittances protect Somali human rights, providing a crucial safety net for Somali households and for the economy as a whole. Perhaps 40 percent of households in Somalia rely on remittances from the diaspora.

In addition, remittances have significant positive macroeconomic effects. Funds sent home by the diaspora through SROs provide a crucial injection of foreign exchange revenue, allowing Somalis to import essential foodstuffs such as oil, sugar, and flour despite Somalia’s almost permanent trade deficit. They are an essential component in the Somali economy.

Remittances are inherently fungible. Senders cannot control what happens to the funds they send once they reach the recipient. They may be sent for one purpose but then used in quite a different way. In part for this reason, these remittance flows are perceived by some counterterrorism and security organizations as a potential risk. Our research and analysis suggests that understanding where and when remittances are most vulnerable to becoming sources of terrorist finance requires an improved understanding of how Somali remittances are organized.

HOW ARE SOMALI REMITTANCES ORGANIZED?

Understanding that SROs are powered by trust in family and national bonds, rather than in abstract concepts such as the market and in formal institutions such as banks, is key. Somali society traditionally emphasizes trust, privacy, and clan identity. Transnational migration, finance, and trade have simply dispersed these indigenous Somali “trust networks” around the world. Because SROs are an outgrowth of transborder family networks, clients trust these organizations to send overseas wages home and to handle payments in crucial business transactions.

One way to think about the Somali remittance sector is as a transnational ecosystem. This ecosystem is a complex community of highly varied organizations that operate within the transnational space of the Somali nation. They participate in this space in numerous locations around the world: within the territory of Somalia and within Somali communities in greater East Africa, Yemen, the Gulf of Arabia, diaspora communities in the countries of the Organisation for Economic Co-operation and Development (OECD), and increasingly India and China.

Internally, these entities are organized in an astonishing variety of ways: as community-based cooperative charitable mechanisms, as highly vertically integrated multinational conglomerates, as financing arms of trading companies or ancillaries to larger foreign exchange houses, and as international franchise networks.

We identify three different but interrelated organizational types.

- 1. Charity and family networks.** These SROs are the simplest, collecting remittances at the ends of extensive transnational Somali diaspora networks. They are often structured as informal charitable cooperatives sending small amounts home to provide income support and charitable donations.
- 2. Retail entities.** These SROs handle a greater volume of cash, consolidate funds, and may interface with the formal financial sector through operation of a bank account. They often move funds from the outer extremity of the network to the center. They operate through numerous agents who solicit or receive remittances, consolidate them, and organize them for transmission or payment out at the payment end. This model has low barriers to entry because it relies heavily on existing social capital, mainly family and clan ties, to build distribution networks. As these retail SROs

grow to handle larger amounts of financial flows, they are more likely to become visible to regulators and are forced to work across traditional clan lines. Retail remittance organizations make their profits first through commissions on remittances, usually set around 3–5 percent of the funds remitted, and then through exploitation of exchange rates. This tier is largely characterized by high levels of competition between various SROs who operate on thin margins.

3. Commercial clearinghouses. These SROs are often situated within foreign exchange houses and trading houses in Dubai or occasionally Sharjah in the UAE and Eastleigh, in Nairobi, Kenya. They serve as a clearinghouse and switchboard, connecting bundled remittances from retail networks and routing them to their final destination. Their access to large remittance flows allows them to engage in currency arbitrage and complex trade financing. Commercial clearinghouses necessarily do very substantial business outside their clan networks and may form commercial partnerships across clan lines to maximize payment-out coverage in Somalia and beyond. Clearinghouses are often situated in geographic trading hubs and are players in global foreign exchange markets. They often oversee the settlement processes of Somali import/export transactions. Commercial clearinghouses frequently get the largest pieces of the commission from retail remittance and commercial transactions, typically taking 42–45 percent.

These three types of SROs thus fit together in an extensive global network of back-to-back currency swaps. These are organized around two major streams: one constituting a “bank wire stream,” swapping OECD currencies for U.S. dollars in the central hub, usually Dubai, and the other swapping those dollars for local currencies, such as Somali shillings, Kenyan shillings, and Djiboutian francs, often through trade-based transactions into and out of Dubai.

SRO networks typically pass through geographic business hubs, for example in Dubai in the UAE, Nairobi and Eastleigh in Kenya, and increasingly Sharjah, also in the UAE. These hubs play a key role in the informal regulation of these flows by the SRO network itself. Since the collapse of the Somali economy in the early 1990s, these locations have become the destination of Somalis seeking everything from medical services to entertainment and have developed into Somalia’s economic and trade hubs away from the physical geographic area of Somalia, allowing Somalis access to the global economy. Beyond the apparent cultural and religious linkages and close geographic proximity between Somalia and the UAE, these hubs offer a number of additional incentives to businessmen, traders, and financial entrepreneurs, including SRO managers. These include access to trade networks, de facto or de jure tax-free zones, and cheap cargo and shipping options. These hubs provide an interface between the bank wire stream, carrying value from OECD countries to the hub, and what this report has labeled the “trade stream,” moving value through trade transactions from the hub into Somalia and elsewhere in East Africa.

Our research suggests that these broad bank wire and trade streams may be broken down into remittance “corridors,” particular physical or virtual routes along which remittances habitually flow. In the Somali context, because consumer choice in the SRO market appears to be mediated by clan affiliation, with further research, it may be possible to identify the contours of clan influence within the transnationalized Somali political economy.

Mapping Somali remittance corridors holds out the prospect of identifying how and where funds are flowing but not necessarily of predicting how they will be used once they arrive. In other words, it offers a way to map risk, not outcomes. If developed through further research and in collaboration with SRO representatives, such a map or matrix identifying which clans tend to send money through which international corridors might offer a more precise analysis of where at any given time there is a heightened risk of remittances supporting conflict, human rights abuse, or terrorism. That would serve regulators and remitters well because it would allow them to work together to address those risks in a cost-effective manner, for example, by clarifying which specific corridors require heightened attention from regulators and on which Politically Exposed Persons (PEPs) or kinds of linked transactions the SROs and banks should focus their due diligence efforts.

BOX 1. HOW DOES MONEY MOVE TO AND FROM SOMALIA?

AGENT/COLLECTOR – The basic arrangement involves a collector (“agent”) who receives value, usually in the form of cash from a client. The agent is often physically located in a small kiosk inside an Internet café, mobile telephone service center, or foreign exchange bureau somewhere accessible to a Somali migrant community.

“INFORMATION TRANSFER” and **“VALUE TRANSFER”** – Remittances follow a three-step process. First, the sending agent communicates information instructing the paying-out agent, either directly or through one or more intermediaries, to make the payment in the stated amount to the intended recipient. This usually occurs very quickly (less than 24 hours later) via telephone, radio, SMS, e-mail, or instant messaging. Second, the sending agent will receive and

consolidate several remittances at the send point before depositing these amounts into a bank account, possibly through a “head agent,” at some point organizing a bulk value transfer to a central bank account affiliated with the central processing unit or clearinghouse of the company or group, often in Dubai. Some time may elapse between these steps. Third, at some point the various agents in the network will settle any debts between them resulting from the first and second steps. This may happen through bilateral or frequently multilateral settlement. It often involves the transfer of value from the clearinghouse to the paying-out point, in many cases involving trade financing mechanisms.

TRADE STREAM – Value is transmitted from the clearinghouse to the paying-out point through trade transactions. The clearinghouse, usually in Dubai, will sell value previously remitted by the sending agents to traders, who use those funds to settle purchasing contracts, often in foreign currencies, especially U.S. dollars. These traders will then sell their goods in East Africa and use the resulting funds to pay the paying agent in local currencies or U.S. dollars for the currency they purchased from the clearinghouse.

PAYING-OUT AGENT – The agent on the other side of the transaction provides the recipient of funds with payment. Payments are cash or trade based.

See further Figures 1a and 1b on page 20.

HOW ARE SOMALI REMITTANCES REGULATED?

The **second part** of this report offers an overview of how SROs are currently regulated, suggesting that a decade of distrust has created a trust deficit between regulators and SROs. Improving the formal regulation of Somali remittances requires capitalizing on informal trust, turning the social capital within SROs into a basis for strengthened regulation of Somali remittances.

Although SROs generally keep recordkeeping to a minimum, they are in fact highly internally self-regulated through a process of mutual surveillance within the SRO network. Because the SRO network is built on trust and is largely a “closed” network, risks of financial losses are minimized; any misstep by one SRO will quickly be met by that SRO’s exclusion from the network. This setup offers the sender of funds, the consumer, significantly reduced risk of loss. The heightened awareness of network security, particularly as it translates into guardedness against external regulators, is therefore not necessarily the result of having something to hide but is rather the cultural and social norm of doing business.

Regulators often may not see it this way. International efforts to regulate SROs have largely been shaped by attempts to minimize risks of money laundering and terrorist financing. Regulators, apprised by credible and frequent intelligence, are concerned about SROs’ vulnerability to exploitation for terrorist financing and in particular the use of the SRO network in fundraising activities and terrorist operations. Regulators tend to emphasize anti-money laundering/countering the financing of terrorism (AML/CFT) objectives in regulatory activities, rather than such other objectives as promoting development in Somalia, protecting consumers from the risk of fraud or monetary loss, or regulating the supply of foreign exchange. While external regulators are looking at reducing money-laundering and terrorist financing risks, SROs are primarily guarding

against risks to the consumer in sending and receiving funds. A trust deficit therefore arises in the gap between the regulators and SROs regarding the objectives and execution of regulation.

Our research suggests that there is also some evidence of regulatory fragmentation along similar lines at the national level. Security agencies see SROs as representing a degree of risk that is not matched by the resources that other responsible agencies devote to SRO regulation. Those agencies, frequently responsible for financial sector supervision, do not see SROs as a major source of risk to the financial system. As a result, they tend to devote fewer resources to engagement with SROs than security agencies' description of the risks might suggest are warranted.

As a result, SROs tend to experience regulation as somewhat fickle and arbitrary and question whether regulation is proportional to the risk they actually pose. Many of those we interviewed indicated that they feel singled out for excessively heavy and intrusive treatment. They often feel that such regulation is poorly explained to them, complaining, for example, about the lack of Somali-language explanatory materials or explanations of regulatory decisions. As one interviewee said, "What do you get from a license? A headache." The same interview subject, complaining that he spent 80 percent of his time on compliance issues, later stated that "[c]ompliance is killing the business."

The challenge is complicated by the significant cultural, linguistic, and social gaps that exist between staff in regulatory bodies, especially in OECD countries, and the actors within the SRO ecosystem. The result is a pervasive sense of distrust among OECD state regulators and SROs and sometimes perverse results in the implementation of the AML/CFT regime.

Without question, SROs and regulators view the risks associated with the SRO business differently. A large part of the problem, however, seems to be the failure of regulators to convince SROs of the utility and importance of managing these risks, which seems to result from a failure to frame a coherent narrative presenting regulation as in the interest of SROs and to communicate that message consistently across government and across different jurisdictions.

One reason for this breakdown may be the fragmentation of regulatory strategies and responsibilities across different government agencies, leading to a mismatch between statements on the risk involved in SRO business and the resources that government devotes to managing this risk. Few governments have an effective whole-of-government strategy framing common regulatory objectives across government in dealing with SROs.

International efforts in this area have largely coalesced around three different regulatory models: bans, registration, and licensing. Bans are viewed with some skepticism, following the experience with some governments' banning in 2001 of al-Barakaat, one of the largest global SROs at that time and Somalia's largest private employer. The enormous social costs created by the ban and the rhetoric that surrounded the process created a climate of deep mutual suspicion, defensiveness, and even hostility between Somali remitters and regulators in the United States and in OECD states.

The focus is now on registration and licensing, and indeed our research suggests that many jurisdictions are slowly converging around a hybrid of the licensing and registration models. The Financial Action Task Force (FATF) has issued recommendations intended to encourage financial institutions to take steps to protect against terrorist financing. This includes a recommendation, previously known as Special Recommendation VI, that stipulates that all remittance systems should be subject to licensing or registration and should comply with other FATF recommendations. In attempting to interpret and implement the FATF recommendations, discussion at the international level has focused on formalization of the industry and registration. Regulators have pushed SROs to adopt practices resembling those of formalized banks, including implementing know-your-customer (KYC) protocols, carrying out enhanced due diligence for PEPs in Somalia, and providing suspicious transaction reports (STRs).

Despite the administrative burdens involved, many SROs have made considerable efforts in the last few years regarding these practices. Yet, SRO compliance efforts are dogged by the limited resources available to SROs, misunderstanding and mistrust between regulators and SROs, and the difficulty of applying AML/CFT concepts in the SRO context. KYC protocols and STRs, for example, are risk management tools specifically designed for banks and financial institutions operating in the open market with a general clientele; they map poorly onto the business model and environment of SROs, with closed trust networks. This leads to recurring concerns among regulators that SRO KYC efforts are somehow “for show,” especially given the difficulty of applying KYC standards across the different SRO entities involved in a remittance transaction. Similarly, SROs have received little guidance from regulators on how to define and identify a PEP in the Somali context, which is by no means straightforward, given the multiple political institutions and broad family networks. Their resulting difficulties in complying with AML/CFT norms serve to work against the regime’s central objective of risk management. Our research suggests that some SROs move operations across borders to minimize the associated compliance costs imposed by different regulatory regimes. Overly onerous regulatory requirements may risk pushing some SROs, especially smaller retail SROs, away from the formal sector, counterproductively reducing transparency.

One of the biggest challenges in regulating SROs is the role played by private banks. Regulators require banks to assess the AML/CFT risks associated with their clients, creating an incentive for banks not to work with clients they perceive as risky, such as SROs. Some jurisdictions, notably the United States and the United Kingdom, have begun to take some limited steps toward working with banks to provide a more nuanced understanding of the risks associated with different SROs. In the absence of such steps, however, our research suggests that banks in most jurisdictions and in the United States and the United Kingdom remain very shy of engaging with SROs. Increasingly, this is leading to major negative unintended regulatory consequences, in particular the reduction of humanitarian assistance flowing from Somali diaspora communities to affected households through SROs. When banks do engage with SROs, they frequently undertake their own site visits and conduct due diligence activities into the business operations of SROs in order to discharge their own AML/CFT obligations and often pass on the costs to SROs. Yet, our research suggests the information they gather is rarely shared with regulators. Again, the result is a weaker regulatory regime than necessary.

The challenge for regulators is to know what burden different SROs will be able and willing to bear. As suggested throughout this study, that requires an improved understanding of how SROs operate and how regulation interfaces with SROs in practice.

BOX 2. 10 KEY LESSONS FOR REGULATORS

1. EXPLAIN SOMALI REMITTANCE ORGANIZATIONS (SROs) TO BANKS.

Banks play a key role in the SRO industry, as vehicles for wire transfers for accumulated remittance deposits and as proxy regulators for anti-money laundering/countering the financing of terrorism (AML/CFT) efforts. Yet, they often have a poor understanding of how SROs operate. Given their risk-averse culture, some banks will therefore choose not to do business with SROs, which can lead to adverse outcomes such as reductions in humanitarian assistance by diaspora communities. Regulators can help address this problem by working with SROs to undertake outreach to banks to better explain how the SRO industry operates.

2. PROVIDE ACCESS TO MATERIALS IN THE SOMALI LANGUAGE.

Disseminating materials to SROs to communicate compliance obligations in the Somali language can help reduce misunderstanding and mistrust and provide opportunities for improved engagement. Regulators should also consider sending Somali language translators on site inspection visits.

3. PROVIDE WRITTEN EXPLANATIONS OF REGULATORY DECISIONS.

Providing written, timely explanations of reasons for regulatory decisions such as the issuance or nonissuance of licenses, the results of inspection visits, and corrective measures that SROs can implement in their businesses will help create a regulatory partnership between regulators and SROs.

4. CALIBRATE REGULATORY FEES TO THE SIZE OF AN SRO.

Designing and implementing a scale of regulatory fees on the basis of the size of the SRO, either revenues or funds remitted, will help ensure that even the smallest charitable and retail SROs have a realistic chance to participate in the regulatory system and reduce incentives for them to operate underground.

5. OFFER GUIDANCE ON POLITICALLY EXPOSED PERSONS (PEPs) AND SUSPICIOUS TRANSACTION REPORTS (STRs).

It may be difficult to apply existing definitions of PEPs to the Somali context because there are multiple government institutions and family networks that may not map easily onto existing definitions. Working together with SROs to tailor reporting and due diligence guidelines to the Somali remittance context, and to ensure SROs are regularly providing the information that regulators need to help SROs identify PEPs, is a good way to align expectations between regulators and SROs and to strengthen regulatory cooperation.

6. BEWARE OF FALSE POSITIVES IN AML/CFT SOFTWARE.

Many Somali names are similar due to clan affiliation and genealogical linkages. The same name may also have multiple spellings in the Roman alphabet. Software-based due diligence systems inevitably raise numerous false positives, matching client names to those on a blacklist. Close attention by regulators is required to ensure this does not lead to incorrect punitive action.

7. ENCOURAGE TRADE ASSOCIATIONS. Trade associations can serve as a transmission belt conveying norms from government to industry and can help regulators to test and develop new norms and implementation arrangements. In addition, trade associations can help SROs implement their regulatory obligations by providing access to common

resources, such as implementation kits, training sessions, tailored software, and explanatory materials. Trade association groups may also offer a cost-effective way for regulators to engage SROs in dialogue.

8. FOSTER INFORMATION SHARING

WITHIN GOVERNMENT. Information about Somali remittances is often dispersed across multiple regulators within a given jurisdiction (police, intelligence services, development agencies, financial regulators, and immigration and multiculturalism services). Regular meetings to share this information, subject to legal restrictions, can help ensure that multiple regulatory objectives are met and the workings of SROs are better understood across government.

9. WORK WITH REGULATORS IN OTHER STATES.

Regulatory disparities between one state and its neighbors can create incentives for SROs to move their business to other jurisdictions. SROs are highly networked and can easily move operations to neighboring states. Passporting arrangements in EU states also allow some SROs to evade regulatory requirements, weakening the regulator's ability to ensure effective risk management in that jurisdiction. Regulators can address this through improved cross-border cooperation or even working toward regulatory harmonization.

10. BUILD THE CAPACITY OF REGULATORS IN EAST AFRICA.

The ability to ensure that AML/CFT and other regulatory objectives are met will be limited while regulation of SROs in East Africa remains as weak as it is now. States should work together to strengthen the capacity of regulators in East Africa.

RECOMMENDATIONS: CAPITALIZING ON TRUST, FROM CONFIDENCE BUILDING TO STATE BUILDING

One of the key regulatory problems, simply framed, is a lack of trust. SROs do not trust that it is in their interest to bear the regulatory burdens regulators require of them in order to manage AML/CFT risks, and regulators and their proxies—banks—do not trust that SROs are faithfully discharging those burdens. The challenge is to rebuild that trust after a decade of distrust. In the **third part** of the report, we present a number of recommendations concerning how this might be achieved.

Building trust will require coordinated, multijurisdictional efforts by regulators to convince SROs that effective regulation, including to manage AML/CFT risk, is in the SROs' interest. That will require a deliberate and coordinated effort by regulators to reframe the regulatory discussion or, in other words, to incentivize and encourage compliance. They will need to find short-term projects on which they can partner with SROs to build mutual confidence, which in time may blossom into trust.

Regulators and SROs should therefore work together and with a relevant international partner, such as the UN Development Programme or the World Bank, to establish a **Remittance Roundtable Process**. Roundtables would bring together regulators; financial institutions, especially banks; community groups; law enforcement; and SROs to discuss how the potential of Somali remittances might be better harnessed. These roundtables should occur in East Africa, the Persian Gulf, the United States and Canada, the United Kingdom, and Europe and, if possible, within Somalia itself. Each roundtable would bring together local stakeholders to develop practical ideas for ensuring that SROs contribute to peace, human rights, and prosperity in Somalia. The aim of these forums would be to move the discussion past the last decade of distrust and reframe regulatory questions as a partnership intended to minimize the AML/CFT and human rights risks involved in the SRO business and to lay the foundation for future Somali peace and prosperity.

In addition, we believe that trust will be built better and faster if these roundtables provide not just a talkshop, but a forum for joint, practical problem solving. Our second recommendation is therefore that members of these roundtables undertake a **series of joint, short-term concrete projects** to develop the following tools.

- **Outreach tools explaining Somali remittances to banks and other regulators.** A small group of regulators and SROs could work together to produce a set of materials explaining how the industry typically operates to dispel some of the myths that surround it. A cooperative effort to produce and disseminate these materials could significantly build confidence between those engaged in the effort and also among the broader financial and regulatory community about Somali remittances.
- **Risk analysis and early-warning tools.** Regulators and SROs could share information on a recurring basis about which communities in Somalia are most affected by armed conflict and terrorism. This would allow regulators and SROs to develop a more detailed understanding of where AML/CFT and human rights risks are present at any given time in the global Somali remittance network, allowing them to more efficiently allocate their resources for KYC and enhanced due diligence efforts, especially around PEPs.

Finally, our research suggests that SROs represent an untapped source of social trust and financial capital for the reconstruction of Somalia. We identify **three long-term, concrete projects** that the international community could undertake in cooperation with SROs: Diaspora Bond offerings to fund local development projects, a Mobile Financial Services Plan, and a Somali Financial Reconstruction Roadmap.



The boundaries and names shown and the designations used on this map do not imply official endorsement or acceptance by the United Nations.

Introduction

SOMALIS REMIT MONEY HOME FOR MANY REASONS. Some Somalis send money to family members and fellow nationals to support them through famine, war, and drought and provide a real and substantial bulwark to protect their human rights in the process. At roughly \$1.0–1.5 billion remitted annually,¹ Somalia is among the most heavily remittance-dependent economies in the world.² Other remittances are sent home for investment purposes. They offer a channel for self-help by the transnationalized Somali community, a vehicle for Somalia's economic recovery and sustainable development unburdened by foreign debt or dependency. For a third group, remittances are first and foremost a duty, a way to maintain a sense of community and solidarity in an age of global migration and for acting on clan and political affiliations across borders. For Somali import/export traders, remittances are the source of the foreign exchange they need to conduct business in regional trading hubs such as Eastleigh in Nairobi and Dubai in the United Arab Emirates, without which the import of everything from basic foodstuffs to luxury cars into Somalia would be impossible. Yet for many foreign security agencies and financial regulators, Somali remittances represent a mysterious and somewhat baffling alternative international financial infrastructure, which seems opaque to external supervision and vulnerable to exploitation for money laundering and financing terrorism.

Somali remittances probably play all these roles. How they are regulated thus depends on which of these risks and opportunities regulators see, as well as which they choose to privilege. In the last decade, regulators have focused primarily on the risks involved in Somali remittances, in particular the risks of money laundering and financing terrorism. Some regulators at times have taken steps to shut down Somali remittance organizations (SROs) altogether. Following their lead, banks in many jurisdictions are now deeply reluctant to do business with these organizations. In the United States, the decision by Sunrise Community Banks in Minnesota in December 2011 to stop processing Somali remittances for fear of violating U.S. counterterrorism laws threatened to cut off the last channel for the U.S. Somali community to send remittances to communities in Somalia suffering from ongoing drought, displacement, and the effects of continuing armed conflict.³

SROs face a serious trust deficit on the part of formal regulators and banks who serve under the existing anti-money laundering (AML) regime as a kind of informal regulator. At the same time, the steps taken by regulators and banks over the last decade have created a deficit of trust among the Somali community, making it more difficult for regulators to work with the Somali community and achieve effective regulation. In this study, we ask how those trust deficits might be overcome.

1. Mohamed Abshir Waldo, "Somalia Remittances: Myth and Reality," in *Remittances and Economic Development in Somalia: An Overview*, ed. Samuel Munzele Maimbo (Washington, D.C.: World Bank, 2006), p. 20. This figure is discussed and confirmed in part 1 of this report.

2. Joshua Keating, "Who Gets the Most Remittances?" *ForeignPolicy.com*, 9 May 2011, http://blog.foreignpolicy.com/posts/2011/05/09/who_gets_the_most_remittances.

3. Mark Tran, "Aid Groups Lobby U.S. Not to Shut Off Remittances to Somalia," *Guardian*, 4 January 2012, <http://www.guardian.co.uk/global-development/2012/jan/04/aid-us-remittance-money-somalia>.

The answer we present in this report is that trust deficits between regulators and banks and remitters might be overcome by capitalizing on the trust that already exists within the Somali remittance system and that allows it to operate as it does. That requires a more nuanced understanding of how Somali remittances work and an identification of opportunities for building on that trust through a confidence-building process we describe in part 3.

Decades of labor and refugee migration to the Persian Gulf, Europe, and the United States, combined with long-standing traditions of Somali entrepreneurialism, have turned the Somali political economy into one of the most highly transnationalized in the world.⁴ At the same time, more than two decades of war, human rights abuse, and drought have left central government institutions weak and their real power over parts of the Somali state's territory nonexistent.⁵ Somali politics, economy, and society are organized on the basis of traditional institutions such as clan and *jilib* (which we discuss later), so state and international regulators find them difficult to read and even more difficult to regulate. Money and power, trust, and risk operate in the Somali political economy in ways with which Western bureaucratic structures struggle to cope.

This report aims to clarify how Somali remittances work and to identify areas where regulators, banks, and remitters might work together to build trust and strengthen the Somali remittances sector. Drawing on extensive desk research, 27 interviews with SROs and regulators, and 14 responses from national financial intelligence units (FIUs) to an online questionnaire, the Center on Global Counterterrorism Cooperation with the support of the Royal Government of Denmark set out to investigate the regulation of Somali remittances and to consider how it might be strengthened. This report explores how Somali remittances are organized, how they are regulated, and how we might strengthen that regulation and better harness the potential of

Somali remittances to underwrite Somali peace, prosperity, and human rights.

In part 1, this report explores the emergence and development of SROs, organizations run by Somalis or that operate in Somalia or Somali communities that conduct nonbank financial transfers involving cash payments at one end of the transaction (payment in or payment out). SROs have emerged out of and remain intertwined with a number of traditional and mercantile financial practices, most importantly the system of financial solidarity within family groups known as *jilib* and the traditional Indian Ocean trade finance vehicle known as *hawala* (in Arabic, “transfer”; *xawilaad* in Somali). In the absence of an effective formal banking sector in Somalia, SROs serve as the primary vehicle for the diaspora's family income support; charitable donations, including *zakat*; small-scale business development; and venture capitalism. This report explores the positive macroeconomic, human rights, and developmental impacts of remittances, including the support they provide to livelihoods and macroeconomic resilience because of their countercyclical nature and the access to foreign exchange that they afford. It also looks at the intersection of remittances and politics, serving potentially as a means to finance militancy as well as peace.

Yet, especially for those who work within them, SROs are much more than a financial and social mechanism tying the Somali diaspora to their homeland, the aspect on which many existing studies focus.⁶ They are a business. They are built on traditional foundations, notably those of *hawala*, but operate in a modern setting. SROs now operate as a component in larger, globalized foreign exchange markets and trade financing systems. Part 1 therefore also attempts to explain how this business is organized. Our report identifies at least three types of SRO, operating at interlocking levels of business—charity and family networks, retail SROs, and commercial clearinghouses—and explain how they are

4. Laura Hammond et al., *Cash and Compassion: The Role of the Somali Diaspora in Relief, Development and Peace-Building*, December 2011, <http://www.so.undp.org/docs/Cash%20and%20compassion.pdf>.

5. Peter D. Little, *Somalia: Economy Without State* (Bloomington, Ind.: Indiana University Press, 2003); Christian Webersik, “Mogadishu: An Economy Without a State,” *Third World Quarterly* 27, no. 8 (2006): 1463–1480.

6. For example, see Anna Lindley, *The Early Morning Phone Call: Somali Refugees' Remittances* (New York: Berghahn Books, 2010); Cindy Horst, “The Transnational Political Engagements of Refugees: Remittance Sending Practices Among Somalis in Norway,” *Conflict, Security, and Development* 8, no. 3 (October 2008): 317–339.

owned and operated and interface and where they are located. The SRO business emerges as a sophisticated global system of back-to-back currency swaps connected to the Somali import/export market.

The key to how this system has developed and is organized turns out to be trust.⁷ Trust powers the entire SRO business model, from the bottom to the top. SROs not only capitalize on trust, but in a very real sense, they capitalize trust. Trust provides security for moving large values over long distances through cooperation with people that an SRO agent may never meet. Trust allows SROs to undercut formal money transfer businesses and banks. SROs replace the formal system's expensive bureaucratic safeguards, designed for an open market populated by economic strangers, with a closed network constructed out of the social capital and safeguards provided by family and clan membership and the careful system of mutual surveillance that such a closed network allows. As we shall see, SROs in a sense are a huge, transnational, informal self-regulating trust network.

As noted in part 2, the closed, self-regulating nature of this network has proven deeply problematic for external, i.e., state, regulators. Unfamiliar with dealing with or influencing such systems, foreign regulators see the informality of the Somali remittance sector as making it vulnerable to becoming a conduit for corruption, financing criminal, pirate, and terrorist activity and money laundering. They struggle to apply existing norms and mechanisms, especially in the AML area and in countering the financing of terrorism (CFT), to the very different social and institutional context in which SROs operate. Security agencies in particular see a sector fraught with risk. Where remitters see complex Somali remittance networks as a financial arterial system for the Somali body politic, foreign security regulators at times characterize these networks as potentially dangerous underground conspiracies, fuelling crime, terrorism, conflict, and human rights abuses.

A decade of problematic efforts at regulation has unfortunately led to abiding distrust between SROs and regulators.

At times, some regulators have seemed to be unwittingly reprising past imperialist efforts to eradicate hawala systems, all of which evidently ended unsuccessfully. In recent years, there has been some begrudging movement on each side of the equation. Undoubtedly, SROs have made a substantial effort to adapt to the new rules they have faced over the last decade: systems of licensing and registration, adoption of know-your-customer (KYC) protocols, changes in record-keeping, and reporting of suspicious transactions. In addition, regulators seem increasingly to be converging around a hybrid model of registration and licensing that more sensitively calibrates the administrative and compliance burdens that SROs face to different SRO types' sizes and functions.

Yet, as explored in part 2, there are also real questions about the effectiveness of this regulatory approach in practice. The risk management concepts and mechanisms built into this regulatory regime do not map easily onto SROs. To take one example, because the SRO that sends a remittance is often a different legal entity from the SRO that pays it out at the other end of the chain, even if the sending SRO meticulously discharges its KYC obligations, it provides only limited information about where the remittance is being paid out and none at all about how it is used after it is paid. To take another example, what constitutes a "suspicious" transaction may look very different to a regulator, unfamiliar with Somali society and the xawilaad system, and to an SRO. As a result SROs, like other *hawaladars*, are perceived by regulators as underreporting, while regulators, to SROs, appear unnecessarily suspicious of SRO transactions.

The result is not only a regulatory system of patchy effectiveness but abiding distrust between regulators and remitters. Regulators' knowledge of where and how Somali remittances are ultimately paid out remains weak. That appears to reinforce existing suspicions and distrust. Moreover, a pattern of regulatory fragmentation emerges: even within one state, different regulatory bodies approach SROs with vastly differing regulatory objectives in mind, from integration of the Somali community into the host nation's body politic

7. For detailed analysis of the role of trust in the hawala networks of Afghanistan, see Edwina Thompson, *Trust Is the Coin of the Realm: Lessons From the Money Men in Afghanistan* (New York: Oxford University Press, 2011). For similar analysis regarding India, see Roger Ballard, "Hawala Transformed: Remittance-Driven Transnational Networks in the Post-Imperial Economic Order," 2004, <http://www.casas.org.uk/papers/pdfpapers/transformed.pdf> 2004. Both works have provided crucial insight and guidance for this report.

to consumer protection, prudential considerations, and countering terrorism. There is often a mismatch between security agencies' perception of risk and the resources that financial regulators (focused on macroeconomic and prudential considerations) devote to regulating SROs, based on a lower perception of risk posed by SROs (since financial regulators focus on a different type of risk). As a consequence, SROs frequently experience regulation as disjointed, arbitrary, opaque, and thus disproportionate to the goals toward which they perceive it being oriented.

The central argument of this study can be captured in the idea that improving the regulation of Somali remittances requires capitalizing on trust, turning the social capital within SROs into a basis for strengthened regulation of Somali remittances. In part 3, this report considers how this might be achieved.

First, the report proposes a Remittances Roundtable Process designed to build trust. This would bring together regulators; financial institutions, especially banks; community groups; law enforcement; and SROs to discuss how the potential of Somali remittances might be better harnessed. These roundtables should occur in East Africa, the Persian Gulf, the United States and Canada, the United Kingdom, and Europe and, if possible, within Somalia itself.

Second, we recommend that participants in these roundtables also consider a set of joint, short-term, concrete projects to foster improved trust between regulators and SROs. The report proposes a short-term focus on joint outreach, joint risk analysis, and joint early warning, not only around AML/CFT norms, which remain contentious, but also around shared human rights due diligence obligations, as recently set out in the UN Guiding Principles on Business and Human Rights.⁸

Third, we identify a series of long-term Somali state-building projects that the international community should consider, in which Somali remittances might play a central role. In its

recent 2011 World Development Report, the World Bank argued that short-term confidence-building measures between former adversaries are necessary to put conflict-affected states on the path to long-term recovery.⁹ Efforts to improve the regulation of Somali remittances offer just such an opening. The Somali remittance sector wields immense power within the Somali nation and economy. It should be engaged as a key partner for the political and economic reconstruction of that country and not treated solely as a source of risk. SROs offer a ready-made reservoir of trust and interclan cooperation, out of which a more stable political-economic settlement might be generated. SROs retain a close relationship with clan structures and the system of financial solidarity within jilib groups. It was traditionally formal agreements between those groups that structured the Somali social contract (*xeer*). An agreement among SROs about how to work together on Somali financial reconstruction and related issues, based on *xeer*, might provide the basis for broader interclan cooperation around regulatory and revenue-sharing issues. In time, this could offer a more effective path to state building in Somalia.

Some specific, concrete projects that the United Nations, World Bank, and states could use to encourage such cooperation include a Diaspora Bond offering, a Mobile Financial Services Plan, and a Somali Financial Reconstruction Roadmap.

Methodology

This study reflects research conducted part-time over eight months during 2011. We began with a detailed literature review of existing governmental, intergovernmental, academic, civil society, private sector, and media analysis of Somali remittance practices. We focused on the last 10 years because regulation of the sector has changed so substantially since 9/11. On the basis of this literature review, we

8. UN Human Rights Council, *Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework*, A/HRC/17/31, 21 March 2011.

9. World Bank, *Conflict, Security and Development: 2011 World Development Report* (Washington, D.C.: World Bank, 2011), http://wdr2011.worldbank.org/sites/default/files/pdfs/WDR2011_Full_Text.pdf.

then conducted 27 interviews with 41 individuals (see appendix 1) using a selective snowballing, or “reference chain,” sample and an unstructured interview methodology, although research questions were informed by our desk research. The development of this sample was facilitated by a consultant already trusted by the SRO community and by cooperation with the Danish FIU, both of whom provided the necessary introductions to key links in the chain. We built a sample that

- included interviews with multiple actors within three different remittance “chains” stretching across Europe, North America, the UAE, and East Africa;
- included interviews with multiple levels of the SRO system (family network, retail SROs, and commercial clearinghouses);
- included a small sample of non-Somali operators working in the same space, as a point of comparison and contrast;
- included SROs working in a broad cross-section of jurisdictions and subject to a variety of regulatory models: Australia, Denmark, India, Kenya, the Netherlands, Norway, Saudi Arabia, Somalia, Sweden, Tanzania, the UAE, Uganda, the United Kingdom, and the United States; and
- included interviews with regulators from East Africa and Europe.

Based on the data we collected in these interviews, we developed an online questionnaire that was circulated to FIUs around the world with the assistance of the Danish FIU (see appendix 2). We received responses from 14 FIUs on three continents (see appendix 1).

All interviews and the survey were conducted on the basis of anonymity. Accordingly, all our references to these interviews and survey responses refer only to an interview number (e.g., personal interview no. 1) or survey response number (e.g., survey response no. 2). Anonymized descriptions of these interview subjects are provided in appendix 1, together with a list of the countries that replied to the FIU questionnaire (with an explanation of how those responses have been anonymized). In a very limited number of instances

necessitated by security concerns, we have withheld all reference data.

Finally, a first draft of the report was workshopped in Copenhagen on 8–9 December 2011 with SRO representatives, national regulators, regional regulators, money transfer association representatives, and independent and academic experts.

Terminology

Arabic and Somali terms are explained in the Glossary and Acronyms list. Throughout this report, for the sake of simplicity, “Somali remittance organizations” or “Somali remitters” are referred to as SROs. Yet as stressed in part 1, this sector is far from homogeneous. It includes a wide range of organizations operating on very different business models, from community-based cooperative charitable mechanisms to highly vertically integrated multinational conglomerates. Some operate as classic hawalas. Others are beginning to resemble online banking outfits, and others focus on trade finance, using remittances to service a larger *franco valuta* system or to participate in global foreign exchange markets.

Partly because of this complexity, terms such as “alternative remittance systems,” “informal funds transfer,” “informal money transfer systems,” and “informal value transfer systems”¹⁰ are avoided in this report. They unhelpfully reinforce the perception that remittance practices and organizations exist apart from, rather than intertwined within, more formalized financial transactions. The reality is more complex: money (and power) move backward and forward between the informal and formal realms, sometimes matching formal and informal vehicles together in surprising ways.

Despite the heterogeneity in the sector, a number of characteristics unite SROs. Chief among these is their “Somali-ness,” their access to the Somali language and Somali clan and family networks that ultimately makes them an identifiable

10. See Nikos Passas, *Informal Value Transfer Systems, Terrorism, and Money Laundering*, National Institute of Justice, November 2003, <http://www.ncjrs.gov/pdffiles1/nij/grants/208301.pdf>.

system embedded within the larger global financial system. For that reason, in this report the simple catchall term “Somali remittance organization” is used. This connotes organizations that are run by Somalis or operate in Somalia or Somali communities that conduct nonbank financial transfers involving cash payments at one end of the transaction (payment in or payment out).

Difficulties for and Limitations of the Research

The study was constrained by a number of difficulties, which resulted in several limitations. First, researching transnational remittances is inherently resource intensive. Remittance networks exist across large distances. Identifying and gaining access to different nodes within the network takes significant time and money. Despite very generous support from the Royal Government of Denmark and assistance from numerous friends, especially in East Africa, who facilitated this access, our resources were not unlimited.

Due to logistical considerations, we conducted interviews with individuals that work for SROs in North America and Somalia in locations other than in North America and Somalia. This choice understandably limits the generalizability of the research presented here.

Second, people are reluctant to talk about this subject. Frequently, cultural and linguistic barriers confront Western researchers trying to understand the very private world of Somali remitters, especially in the post-9/11 context. Less noticed is the difficulty in getting regulators to talk about this topic, given the operational secrecy and the diplomatic sensitivities that surround this issue.

We sought to overcome both sets of barriers by using gatekeepers—individuals already trusted by the regulator and remitter communities. These gatekeepers introduced us to interview and survey subjects and helped us build rapport. Nonetheless, the absence of certain key jurisdictions from our formal questionnaire sample, notably Australia and the United States, represents another limitation to the research,

although we did engage with U.S. officials and SROs operating within the United States in other parts of our research. Yet, we do not have any particular reason to think that SROs operate radically differently in those places or that they are regulated in a radically different way than is discussed here.

Implications of the Research Beyond Somali Remittances

Just as it is important to consider the limitations of the research, so it is worth noting the potential implications of the research beyond an examination of Somali remittances. The extremity of violence, drought, and poverty in Somalia leads to it often being treated as an “extreme” case with few implications for broader policymaking. No other state, it is often said, is so “failed” as Somalia, so it would be bad policy and regulatory decision-making to design responses for other cases based on what is needed for Somalia. Yet although at one level the study is deeply motivated by an appreciation of the need for contextual analysis, this report suggests that our analysis may hold much broader lessons for policymakers and regulators.

First, the study has implications for our understanding and regulation of the broader hawala system. As the economic power of the Indo-Pacific region rises, we can expect the ancient trade financing mechanisms of the Silk Road, from hawala to *hundi* to *fei qian*, to become even more important mechanisms of global finance. That makes understanding how they operate and interact with different regulatory models a question of not merely academic but also increasingly strategic interest.

Second, the study has obvious implications for the international community’s engagement with financial systems in Somalia as well as the broader Horn of Africa. Our research suggests that SROs are playing a key role as a facilitator of trade financing into Somalia and as an important financial mechanism in the broader informal/illicit economy of East Africa and the Horn, especially where formal banking infrastructure is either brand new (e.g., South Sudan),

undergoing rapid change from a command economy system (e.g., Ethiopia) or deeply intertwined with the informal economy (e.g., Kenya). SROs are a key provider of foreign exchange in each place and thus play an important role in integrating these informal economies into global financial and trading systems.

Third, as discussed at more length in part 3, because the study focuses on the most fungible form of power—money—it also offers insights and ideas for the international community’s broader approach to peace and security in East Africa and the Horn. Understanding SROs offers a way into understanding the often opaque political economy of the region, given the key role that cash financing plays in the region’s patronage politics and interethnic competition and cooperation.¹¹ Analogously, discussions of regulation of SROs and other remittance providers are essentially discussions of regulating power within that informal political economy.

Fourth, the study may offer some interesting departure points for a discussion of the relationship between due diligence in the context of AML/CFT and due diligence in the context of human rights. The UN Human Rights Council recently unanimously endorsed the Guiding Principles on Business and Human Rights,¹² which recognize that states have a duty to protect human rights in their regulation of businesses, including banks and other financial actors, and that those banks and financial actors and other businesses themselves have a “responsibility to respect” human rights. That term is officially understood to mean that businesses must, *inter alia*, have due diligence processes in place to identify, prevent, mitigate, and account for negative human rights impacts with which they are involved.¹³ Larger banks, including Barclay’s Bank, are now turning their minds to the question of how these human rights due diligence obligations may intersect with and be discharged by their existing AML/CFT due diligence infrastructures. AML/CFT due diligence by banks and with SROs may have an important part to play in helping banks discharge their

responsibility to respect human rights in Somalia. Furthermore, learning how to integrate the two forms of due diligence in this field could hold significant benefits for other areas of banking and financial practice.

Fifth, the study may offer some insights of relevance to even broader policy and theoretical discussions regarding the role of diasporas in peace-building and development, about the role of private actors in international relations, about the globalization of previously local trust networks, and about the intersection of transnational finance with local politics and conflict. As the *2011 World Development Report* makes clear, in the future, effective conflict management, human rights, and development policies seem likely to require that more attention be paid to the transnational organization of finance, violence, and legitimacy.¹⁴ The complex problem of Somali remittance regulation should thus be treated less as an extreme outlier among contemporary cases and more as a harbinger of things to come. The lessons we learn from regulating Somali remittances today may have far broader application to the highly networked and globalized diaspora populations and cross-border financial practices of tomorrow.

11. Personal interview nos. 17 and 21.

12. UN Human Rights Council, *Guiding Principles on Business and Human Rights*.

13. *Ibid.* (Guiding Principle 15).

14. World Bank, *Conflict, Security and Development*.

1. How Are Somali Remittances Organized?

“The key to the whole thing is trust.”¹⁵

THE SOMALI REMITTANCE SECTOR IS NOT A homogenous system. It is better thought of as an ecosystem, a complex community of highly varied organizations that all operate within the transnational space of the Somali nation. They participate in this space in numerous locations around the world—within the territory of Somalia and within Somali communities in greater East Africa, Yemen, and the Gulf of Arabia; in diaspora communities in the countries of the Organisation for Economic Co-operation and Development (OECD); and increasingly in India and China. Internally, these entities are organized in an astonishing variety of ways: community-based cooperative charitable mechanisms, highly vertically integrated multinational conglomerates, financing arms of trading companies or ancillaries to larger foreign exchange houses, or international franchise networks. Some move value through a classic hawala system. Others resemble online banking outfits or focus on trade finance, using remittances to service a larger franco valuta system or in a manner similar to the traditional European financial vehicle of bills of exchange.

Effective regulation of such a diverse sector requires careful attention to what differentiates and what unites such organizations. This section of the report is based on extensive desk analysis, field interviews, and an online survey of regulators.

It presents an explanation of how this ecosystem of Somali remittances works, in the process identifying these differentiating and unifying factors.

A Traditional System in a Modernized Setting

Today’s SROs are the result of decades of adaptation of traditional financial practices within the Somali nation to modern settings. Remittances are not just a financial mechanism; they are an expression and reproduction of familial and clan ties and other social bonds, deeply rooted in tradition.¹⁶

Somali society is traditionally nomadic, with “nuclear” family units (parents and children) often spending sustained periods dispersed between rural and urban communities, intermixed with other nuclear family units from the same clan or lineage group.¹⁷ The circulation of assets and value within these distributed networks was not necessarily considered a discrete market-based transaction (a donation, a loan, or an investment) as it might be in more modernized societies.

15. Personal interview no. 21.

16. See Lindley, *Early Morning Phone Call*; Sally Healy and Hassan Sheikh, *Somalia’s Missing Million: The Somali Diaspora and Its Role in Development*, UN Development Programme, March 2009; Thompson, *Trust Is the Coin of the Realm*.

17. Ioan M. Lewis, “Visible and Invisible Differences: The Somali Paradox,” *Africa* 74, no. 4 (November 2004): 495.

Instead, value frequently circulated within these social groups as part of a larger social and, in some senses, financial contract. Somali clans are traditionally subdivided into sub-clans, primary lineages, and “*diya*-paying” groups. Crucially, the *diya*-paying group (*jilib* or *bah*) is the most stable and important political and social unit. A group of between several hundred to more than a thousand families from the same clan, its members are bound by shared obligations of common defense, payment of blood compensation, and, crucially for our purposes, mutual financial and material aid. One SRO director with whom we discussed *jilib* described it as a form of social “insurance.” There is thus a long-standing Somali tradition of trust-based financial transfers over large distances through family networks. The association of Somali families into *jilib* groups was itself the basis for the Somali social contract and political system; *jilib* groups formed alliances through *xeer*, a kind of customary treaty or contract.¹⁸

Somewhere along the way, Somalis interacted with and adopted the *hawala* system of financial transfer that underwrote much Indian Ocean trade. The *hawala* (Arabic for “transfer”) system involves the aggregation and cancellation of debts by designated, trusted intermediaries—a much safer arrangement than carrying hard cash over long distances. The export of livestock, charcoal, bananas, and other goods drew the Somali trading community into this system, with Somali traders using transfers through the *xawilaad* system, as it is called in Somali, based on transfers through their own *jilib* and broader clan networks as part of their import/export business.

Over the course of the last 50 years, this system has adapted to meet a variety of other financial needs. When men from Somaliland in northwest Somalia, mainly from the Isaaq

and Darod clans, travelled overseas with the British merchant navy in the 1940s and 1950s, *jilib* networks and the *xawilaad* system provided a highly mobile, efficient, and cheap way for them to send money back to their families. Growing hostility between the Isaaq clan and Siad Barre’s regime led to a wave of emigration that entrenched these networks in Somali communities in the United Kingdom and other OECD countries. In subsequent decades, as the oil boom in the Middle East drew Isaaq and other Somali clans to the Persian Gulf to serve as migrant labor, Somali *xawilaad* networks became entrenched in Yemen, Oman, Saudi Arabia, and later the UAE.¹⁹ Under pressure from foreign creditors and donors, Barre agreed in 1977 to the institution of the *franco valuta* system, which relaxed Mogadishu’s foreign exchange controls and allowed importers to purchase imports with funds remitted by the 250,000 Somalis now working overseas.²⁰ As Will Reno explains,

The official aim of the policy was to relieve a shortage of basic goods while tapping illicit imports of hard currency estimated to top \$350 million into legal channels that could benefit the country’s depleted treasury. By 1985 remittances to Somalia alone totaled an estimated \$338 million, about fifteen times the entire wage bill for the country’s formal sector. Northerners contributed disproportionately to these remittances, reflecting the tendency of politically marginalized people to search for work in the Persian Gulf and further afield.²¹

Northern roots in Somalia’s remittance ecosystem thus run deep, especially among the Isaaq clan in Somaliland and Darod clan in Puntland. The *xawilaad* system thus has a tradition of sustaining political autonomy for Somali clans and has never been successfully regulated by a central power.

18. See Ioan M. Lewis, *A Pastoral Democracy* (New York: Oxford University Press, 1961), p. 4; Jama Mohamed, “Kinship and Contract in Somali Politics,” *Africa* 77, no. 2 (Spring 2007): 226–249; Ismail I. Ahmed and Reginald Herbold Green, “The Heritage of War and State Collapse in Somalia and Somaliland: Local-Level Effects, External Interventions, and Reconstruction,” *Third World Quarterly* 20, no. 1 (February 1999): 114, http://www.cja.org/downloads/Heritage_of_war__state_collapse.pdf; Paolo Contini, “The Evolution of Blood-Money for Homicide in Somalia,” *Journal of African Law* 15, no. 1 (1971): 77–84.

19. Personal interview no. 22.

20. See generally Vali Jamal, “Somalia: Understanding an Unconventional Economy,” *Development and Change* 19, no. 2 (April 1988): 203–265.

21. William Reno, “Somalia and Survival in the Shadow of the Global Economy,” *Somaliland Times*, no. 64 (12 April 2003), <http://www.somalilandtimes.net/2003/64/6401.htm>. See Norman Miller, “The Other Somalia: Illicit Trade and the Hidden Economy,” *Horn of Africa* 5, no. 3 (1982): 3–19.

Barre's manipulation of the franco valuta system, including by linking import licenses to patronage politics, contributed to continued northern resistance to his rule, which culminated in the northern clans' armed revolt against his regime in the 1980s.²² It was a short step for the formalized franco valuta system to be transformed into an entirely informal system similar to the bills of exchange used by Italian and other European bankers, who were in turn adapting Arabic hawala practices, in the early modern period. A bill of exchange involves a written order by one person to another, usually the bank, to pay the bearer of the bill a specific sum on a specific date, similar to the contemporary checking system. It separates money transfers into two distinct steps: an "information transfer" to a third party who then makes a payment to the second party on behalf of the first and a later "value transfer" that settles the debt between the first and third parties. Modern hawalas and SROs have simply adapted this system. They have replaced the paper bill of exchange in the information transfer with modern communications—satellite telephones, fax, e-mail, SMS, and instant messaging. Also, they have found new vehicles for the value transfer, especially through trade-based financing. Where they differ from modern banks is not so much in this separation of flows of information and value, but more in their reliance on trust within a closed network and not bureaucratic checks and safeguards in an open market as the basis for the value transfer and consequently for their business model.

Indeed, in Somalia it is frequently difficult to tell SROs and banks apart. With the de facto deregulation of the Somali remittance system in the 1980s and early 1990s, xawilaad and remittance organizations began to play a similar role to

that traditionally played by banks. They served as commercial intermediaries and credit reserves for an increasingly wide range of charitable, retail, and commercial transactions.²³ They became the primary vehicle for Western businesses, humanitarian agencies, and the United Nations to move funds into and around Somalia.²⁴ They still play this role for most international and nongovernmental organizations (NGOs) working inside Somalia.²⁵ Traders began using them as short-term banking facilities, placing funds with them as short-term deposits, often for withdrawal in a foreign jurisdiction, to avoid the costs and dangers of travelling with large sums.²⁶ Unsurprisingly, the remittance network quickly became a central mechanism for financing rebel militias and armed groups and for moving funds between family members displaced and dispersed by the resulting armed conflict.²⁷

One of those companies, originally founded in Burao in Toghdheer province and now in Somaliland, became a major service supplier to refugees in camps in Ethiopia's Ogaden province. Originally a trading company focused on labor migrants in the Persian Gulf region, this company, called Dahabshiil (Gold Smelter), adapted new technologies, particularly high-frequency radio and satellite telephony, to align the xawilaad system to these new circumstances.²⁸ Experiencing rapid success, Dahabshiil is now the largest SRO, with more than 24,000 agents collecting remittances in 144 countries and significant cross-sectoral investments in telecommunications and healthcare. In Djibouti, Dahabshiil has even opened a formal bank.

With Barre's fall in 1991, formal banking systems and centralized regulatory arrangements for all intents and

22. Reno, "Somalia and Survival in the Shadow of the Global Economy."

23. See further Ismael Mahamoud Houssein, "Contraintes institutionnelles et réglementaires et le secteur informel a Djibouti," Université de Paris 12 – Val de Marne, 19 September 2008, pp. 195–197, http://tel.archives-ouvertes.fr/docs/00/55/79/89/PDF/These_Mahamoud.pdf.

24. See Anna Lindley, "Between 'Dirty Money' and 'Development Capital': Somali Money Transfer Infrastructure Under Global Scrutiny," *African Affairs* 108, no. 433 (October 2009): 535; Mo Guled, "UN Refugee Agency Launches Inaugural Somali Community Event in Kenya," *Somalilandpress*, n.d., <http://somalilandpress.com/un-refugee-agency-launches-inaugural-somali-community-event-in-kenya-21828>. The event took place on 16 April 2011.

25. Personal interview no. 19; Hammond et al., *Cash and Compassion*, pp. 55–56.

26. Personal interview no. 1. See KPMG East Africa Ltd., *Feasibility Study on Financial Services in Somalia*, February 2004, p. 17, <http://www.somali-jna.org/downloads/Final%20%20Feasibility%20Study%20%20April-2.pdf>; Abdusalam Omer, *Supporting Systems and Procedures for the Effective Regulation and Monitoring of Somali Remittance Companies (Hawala)*, UN Development Programme Somalia, 2002, p. 11, <http://mirror.undp.org/somalia/Remittance/ssp-hawala.pdf>.

27. Cindy Horst and Mohamed Husein Gaas, *Remittances for Peace? The Transnational Political Engagements of Somalis in Norway*, International Peace Research Institute, 2008.

28. Joakim Gundel, "The Migration-Development Nexus: Somalia Case Study," *International Migration* 40, no. 5 (2002): 269.

purposes disappeared in the Somali economy. Although the Transitional Federal Government and Puntland and Somaliland authorities have all subsequently established financial regulatory institutions, they have little real, independent power to control the Somali economy and remain captive to Somalia's clan-based politics. Puntland-based SROs appear to have specifically resisted attempts by that region's Department of Finance to regulate them.²⁹ Regional banks exist to collect taxes, but they are not used for common banking needs and do not have real authority to standardize fiscal policy.³⁰ The Bank of Somaliland and the State Bank of Puntland provide limited commercial banking services, such as deposit accounts and trade finance.³¹

Somalia remains essentially an "economy without a state."³² In that context, private financial service providers wield significant economic and therefore political power. At the same time, with some 1.0–1.5 million Somalis of a total population of perhaps 7.4 million now living outside Somalia,³³ remittance organizations now provide the financial arteries of one of the most transnationalized societies in the world. SROs are the primary financial service provider in the country for the majority of households and for the whole private sector.³⁴

A System Powered by Trust

The key to understanding SROs is recognition that they are powered by trust in the clan and the jilib and in xeer rather than in abstract concepts such as the market and in formal institutions such as banks.³⁵ Somali society traditionally emphasizes trust, privacy, and clan identity;³⁶ transnational migration, finance, and trade have simply dispersed these indigenous Somali trust networks around the world.³⁷ They have taken their skepticism of central government with them. In Somalia, central government has not traditionally been viewed as an objective guarantor of public goods, but as a potential threat to social groups' welfare and security. As a result, state-guaranteed institutions such as banks and regulators may look comparatively risky when compared with tried and tested social institutions such as jilib and xawilaad.

Somali diaspora communities are frequently "unfamiliar with the concept of banks or banking and do not understand where their money is when it is banked or how safe it is."³⁸ For Somalis, xawilaad are the norm, and Western banks, with their strange unwillingness to trust family networks and their upside-down trust in government institutions, are the abnormal alternative. As hawala researcher Edwina Thompson puts it, "[T]he introduction of liberal economic systems to non-Western societies has indirectly 'informalised' activities that have for centuries been the accepted 'norm.'"³⁹

29. Personal interview no. 10.

30. Samuel Munzele Maimbo et al., "Financial Sector Development in Somalia: Central Banking and Financial Services in an Uncertain Environment," in *Remittances and Economic Development in Somalia: An Overview*, ed. Samuel Munzele Maimbo (Washington, D.C.: World Bank, 2006), p. 38.

31. KPMG East Africa, *Feasibility Study on Financial Services in Somalia*, p. 69.

32. Little, *Somalia*; Webersik, "Mogadishu."

33. Healy and Sheikh, *Somalia's Missing Million*.

34. Waldo, "Somalia Remittances," p. 20.

35. Personal interview nos. 1, 11, and 21. For a related analysis of the role of hawala in Afghanistan, see Thompson, *Trust Is the Coin of the Realm*.

36. Saad A. Shire, "Somali Remittance Companies and Their Clients," in *Remittances and Economic Development in Somalia: An Overview*, ed. Samuel Munzele Maimbo (Washington, D.C.: World Bank, 2006), p. 28.

37. On the concept of "trust networks" and their interface with different forms of "rule," see generally Charles Tilly, *Trust and Rule* (Cambridge: Cambridge University Press, 2005).

38. David Rees, "Money Laundering and Terrorism Financing Risks Posed by Alternative Remittance in Australia," *AIC Reports Research and Public Policy Series*, no. 106 (2010), p. 34, <http://www.aic.gov.au/documents/A/8/7/7BA876C9D4-152E-4FDD-93BB-3F98F8C5ED70%7Drpp106.pdf>.

39. Thompson, *Trust Is the Coin of the Realm*, p. 250.

In the aftermath of the collapse of the Somali Central Bank under Barre, many Somalis lost their investments, and today, there is general distrust of state banks.⁴⁰ Why would a Somali trader leave his money sitting precariously with a financial institution in the capital, run by a member of a clan traditionally opposed to his own, rather than ensuring that the value of his money passes straight on to its intended beneficiaries within his own clan, deep in the Somali highlands, through a xawilaad system? Why should a Somali refugee, with his experience of government as a predator, trust an institution such as a bank that focuses more on whether he has a government-issued (and easily forged) ID card than whether he can answer questions about his clan and lineage relations? Seen in this light, regulation becomes more a matter of social trust than of state validation.

Trust in the family and clan is at the heart of the business model, operations, and growth of any SRO, no matter what shape it may take. That trust gives a particular organization its legitimacy among new and potential clients and, within the network, allows one agent confidently to move value to another on the far side of the world, assuming that the network will later settle the resulting debt. That trust keeps an SRO's due diligence and operating costs down, allowing it to service communities that formal banks cannot or will not because margins are too low, and underpins and underwrites interorganizational cooperation through Dubai-based clearinghouses. Consequently, it is OECD regulators' misapprehension of how trust works within the system and their assumption that it is somehow less effective or acceptable than legal contract that underpins the antagonism between regulators and remitters.⁴¹

In a financial sense, trust generated by family and clan ties provides the social capital that substitutes in the SRO model for financial capital in the Western banking system. SROs handle risk not through capital reserves, detailed KYC due diligence arrangements, or insurance or hedging arrange-

ments, but through reliance on preexisting trusted networks and a system of careful mutual surveillance that enforces standards within that network.

[T]he art of hawala is very easily explained: it is grounded in the implementation of exactly the same processes of consolidation and settlement as those which the formal banking system undertakes, but in which the security of each of the transactions which underpin the whole operation is not underpinned by elaborate and expensive processes of formal record-keeping, but rather through decentralised, informal and self-regulating networks of absolute trust.⁴²

It is access to this trust network that allows an SRO to turn a profit and gives each SRO an incentive to demand high standards from its peers. Underperformance will quickly lead to an SRO's exclusion because it brings the trustworthiness of the whole network into question with clients.⁴³ In other words, each SRO is "a specific local node of a huge self-regulating transnational network."⁴⁴

The centrality of trust to the whole system helps explain why SROs and other *hawaladars* are so guarded against outside intervention. This is not necessarily the result of having something to hide; it is a fierce protection of the social capital on which their entire operating system is built. External interventions that call into question one part of the network's ability to operate in line with the expectations of the rest of the network threaten trust in the whole network. Guardedness against disproportionate or heavy-handed regulation is a kind of decentralized, networked solidarity that protects the delicate, dynamic equilibrium of reciprocity and trust on which the system relies absolutely. This makes trust, including between the regulator and the remitter, absolutely central to effective regulation of this sector.

40. KPMG East Africa, *Feasibility Study on Financial Services in Somalia*, p. 69.

41. Compare William Vtcek, "Alongside Global Political Economy—A Rhizome of Informal Finance," *Journal of International Relations and Development* 13, no. 4 (December 2010): 429–451.

42. Ballard, "Hawala Transformed," p. 25.

43. Personal interview nos. 1, 19, and 22.

44. Ballard, "Hawala Transformed," p. 7.

Why Remit?

Trust has traditionally been at the heart of client motivations for moving money through SROs. Because SROs were born from transborder family networks, clients trusted those organizations to send overseas wages home to discharge their diya and other social and religious obligations and to cover payments in crucial business transactions.

Today, remittances still play these roles in modernized settings. They provide crucial income support; there is a close correlation between receipt of remittances and income.⁴⁵ Perhaps 40 percent of Somali households are dependent on remittances.⁴⁶ Women play a particularly important role, organizing remittances through *hagbad* savings circles.⁴⁷ Remittances also discharge familial and religious obligations (financing weddings, funerals, health care, *hajj* contributions, and other forms of zakat)⁴⁸ and provide microinvestments in the business enterprises of family members.⁴⁹ It is estimated that 12–13 percent of funds remitted to Somalia are for investment purposes⁵⁰ and that 80 percent of startup capital for business is funded through remittances.⁵¹ With more and more members of the Somali diaspora choosing to live and work in two places, moving between Somalia, especially Somaliland, and some foreign location, SROs have become an important channel for expatriate financial transactions, such as moving funds home for residential and commercial

construction projects, investing in relatives' education,⁵² or simply moving funds between Somalia and abroad to finance personal consumption.⁵³ A practice that has its roots in the jilib system has been adapted to a wide variety of commercial, charitable, and social purposes in the context of the Somali nation's transnational social life. For example, many Somalis have been making charitable donations across clan lines to support fellow Somalis affected by the recent drought and ongoing armed conflict. There is a pattern, in particular, of northern Somalis living overseas sending money to support communities, including from different clans, affected in southern Somalia.⁵⁴

What is particularly extraordinary about this system is just how frequently Somalis remit relatively significant amounts of money despite their relative poverty in global terms. Our research suggests that it is not unreasonable to think that Somalis living in northern Europe, including Scandinavia, the Netherlands, Belgium, and the United Kingdom, may be remitting as much as \$300 each per month on average. The Norwegian government has estimated that 38 percent of all Somalis in that country remit every month and two-thirds remit at least once a year.⁵⁵ Given that some parts of these populations are known to live in relative hardship in those host countries,⁵⁶ that has led to a feeling of disbelief and suspicion on the part of some regulators. How could these communities be remitting so much without accessing illicit funds or somehow cheating the system, for example, sending

45. See Hammond et al., *Cash and Compassion*, pp. 49–51.

46. Khalid Mustafa Medani, "Financing Terrorism or Survival? Informal Finance and State Collapse in Somalia, and the U.S. War on Terrorism," *Middle East Report*, no. 223 (Summer 2002): 2–9.

47. Personal interview no. 10. See also Lindley, *Early Morning Phone Call*, p. 79; Mohamed Aden Hassan and Caitlin Chalmers, *UK Somali Remittances Survey*, Department for International Development, May 2008, pp. 35–36, http://www.diaspora-centre.org/DOCS/UK_Somali_Remittan.pdf.

48. Anna Lindley, "Protracted Displacement and Remittances: The View From Eastleigh, Nairobi," *UN High Commissioner for Refugees Research Paper*, no. 143 (August 2007), p. 7, <http://www.unhcr.org/46ea519d2.html>.

49. Personal interview no. 17. See Hammond et al., *Cash and Compassion*; Lindley, *Early Morning Phone Call*.

50. Healy and Sheikh, *Somalia's Missing Million*, p. 18.

51. Hassan and Chalmers, *UK Somali Remittances Survey*, p. 7.

52. Horst, "Transnational Political Engagements of Refugees," p. 334. The receipt of remittances appears to correlate with school attendance. See Anna Lindley, "The Influence of Migration, Remittances, and Diaspora Donations on Education in Somali Society," in *Remittances and Economic Development in Somalia: An Overview*, ed. Samuel Munzele Maimbo (Washington, D.C.: World Bank, 2006), pp. 12–13.

53. Personal interview nos. 1 and 16.

54. We are indebted to Laura Hammond for highlighting this point.

55. Svein Blom and Kristin Henriksen, *Levekår blant innvandrere i Norge 2005/2006*, Statistisk sentralbyrå, February 2008, http://www.ssb.no/emner/00/02/rapp_200805/rapp_200805.pdf.

56. Hammond et al., *Cash and Compassion*, p. 28.

welfare benefits to Somalia that were, as one interview subject put it to us, “intended” for use in the host country?⁵⁷

This perception points to a profound misapprehension of the nature of Somali identity and sense of social obligation, including but not limited to the jilib, and where the practice of remittance fits. All the evidence suggests that Somali households around the world frequently remit at least 10–20 percent of household income in the host country and that this may well be higher in wealthier OECD countries.⁵⁸

Finally, in thinking about why remitters remit, this is only one part of the SRO story, and it may not be the most important from a regulatory perspective if humanitarian and developmental objectives are not the regulatory objective that we privilege. Remittances are inherently fungible. Senders cannot control what happens to the funds they send once they reach the recipient. They may be sent for one purpose but then used in quite a different way. There is evidence of some resentment among the population of Somali remittance senders about misuse of funds they send home, including for *qaat* consumption and political and militant activity.⁵⁹ Perhaps even more important than this, though, is understanding the macroeconomic role that remittances actually play beyond the microeconomic perspective on which remitters’ intentions shine a light.

Economic Impacts and Functions

Remittances protect Somali human rights, providing a crucial “safety net”⁶⁰ for Somali households and for the economy as a whole. Perhaps 40 percent of households in Somalia rely on remittances from the diaspora.⁶¹ One estimate suggests that recipients of remittances in Hargeisa receive as much as an additional 40 percent of their annual income in remittances.⁶² At an economy-wide level, they provide a crucial injection of foreign exchange revenue, allowing Somalis to import essential foodstuffs such as oil, sugar, and flour despite Somalia’s almost permanent trade deficit.⁶³

Their significance comes not only from their scale, but also from other factors. Remittance flows are countercyclical in nature generally⁶⁴ and in the specific case of Somalia.⁶⁵ They are extensive—some claim that SRO networks cover nearly the whole of Somalia⁶⁶—and resilient, withstanding social crises such as war, famine, and tsunamis.⁶⁷ SROs are an important source of employment and income within Somalia and within the Somalia diaspora,⁶⁸ which arguably can contribute to a shortage of skilled workers (those who leave to be remitters) and to a dependency relationship between the remitter and his or her family.⁶⁹

57. Personal interview no. 27.

58. Hassan and Chalmers, *UK Somali Remittances Survey*, p. 17; Hammond et al., *Cash and Compassion*, p. 52; Laura Hammond, “Obligated to Give: Remittances and the Maintenance of Transnational Networks Between Somalis at Home and Abroad,” *Bildhaan* 10 (2010), <http://digitalcommons.maclester.edu/bildhaan/vol10/iss1/11>.

59. Hammond et al., *Cash and Compassion*, p. 53; Hammond, “Obligated to Give”; Lindley, *Early Morning Phone Call*, p. 134.

60. Waldo, “Somalia Remittances,” p. 22.

61. Hassan and Chalmers, *UK Somali Remittances Survey*, p. 12.

62. Anna Lindley, “Migrant Remittances in the Context of Crisis in Somali Society: A Case Study of Hargeisa,” *HPG Background Paper*, 2006, p. 11, <http://www.odi.org.uk/resources/docs/410.pdf>.

63. Ballard, “Hawala Transformed,” p. 16.

64. Ralph Chami, Connel Fullencamp, and Samir Jahjah, “Are Immigrant Remittance Flows a Source of Capital for Development?” *IMF Staff Papers* 52, no. 1 (April 2005): 77.

65. Hassan and Chalmers, *UK Somali Remittances Survey*, p. 6; Lindley, “Migrant Remittances in the Context of Crisis in Somali Society,” pp. 16–17.

66. See Hassan and Chalmers, *UK Somali Remittances Survey*, p. 25.

67. Rob McCusker, “Underground Banking: Legitimate Remittance Network or Money Laundering System?” *Trends and Issues in Crime and Criminal Justice*, no. 300 (July 2005), http://www.apgml.org/frameworks/docs/8/AIC_%202005_tandi300.pdf.

68. Waldo, “Somalia Remittances,” p. 20; Sibel Kulaksiz and Andrea Perdekova, “Somali Remittance Sector: A Macroeconomic Perspective,” in *Remittances and Economic Development in Somalia: An Overview*, ed. Samuel Munzele Maimbo (Washington, D.C.: World Bank, 2006), p. 7.

69. Buri M. Hamza, “The Somali Remittance Sector in Canada,” Osgoode Hall Law School, York University, April 2006, p. 8, <http://www.apgml.org/frameworks/docs/8/Canada-Somali%20remittance%20sector%20-%20Nathanson%20Study%20%28Hamza%29%202006.pdf>.

Somali remittances seem to offer a major development success story.⁷⁰ Two-thirds of them are likely used for immediate consumption, but remittances increasingly go toward new organizations and new development projects.⁷¹ More durable investments include land, housing, or ideally self-sustaining business ventures.⁷² The result is a significant multiplier effect. Typically, more remittances are consumed than are saved, and this consumption has a large multiplier effect.⁷³

How Much Moves?

Somalia is consistently ranked as one of the poorest countries in the world, but our research indicates that roughly \$1.0–1.5 billion is remitted to Somalia each year through SROs, or roughly \$200 for every Somali. With Somali gross domestic product estimated at approximately \$2.4 billion, that makes Somalia one of the most highly remittance dependent economies in the world, meaning that SROs wield immense power. By way of comparison, international relief and development assistance to Somalia in 2009 was just \$517 million, or 33–50 percent of the funds moved through SROs.⁷⁴

Our estimate is tentative. Remittance flows are notoriously difficult to measure, but the figure of \$1.0–1.5 billion emerges consistently out of all the primary and secondary data. Regulators from one OECD member state estimated that \$100–200 million is remitted to Somalia from that part of the world, working out to \$300–500 per Somali resident per month.⁷⁵ Another OECD country pointed to remittances of roughly \$400–500 per Somali resident per month.⁷⁶ However, another OECD country with a similar Somali population and host country economic profile quoted numbers closer to \$150 per Somali per month.⁷⁷ Another OECD country with a similar profile but a perhaps somewhat poorer Somali population (from a different clan and with a different socioeconomic profile in the host country) estimated approximately \$100 per resident remitted per month.⁷⁸ If these estimates are accurate, this would still amount to \$1 billion per year from these locations alone. That conforms with numbers elsewhere. The CIA estimates annual remittances to Somalia at \$1.6 billion,⁷⁹ the World Bank estimates \$825 million,⁸⁰ and others have estimated \$1 billion⁸¹ and \$1.3–2.0 billion per year.⁸² In 2002, one estimate offered that perhaps \$12 million per month was remitted from the United Kingdom, or roughly \$300 per head.⁸³ We also believe that estimates based on “remittances received” tend to underestimate the proportion of remittances that are transformed from monetary to trade-based value transfers, usually in Dubai.⁸⁴ As one senior East African

70. Hammond et al., *Cash and Compassion*.

71. Kulaksiz and Perdekova, “Somali Remittance Sector,” p. 7.

72. Lindley, “Migrant Remittances in the Context of Crisis in Somali Society,” pp. 14–15; Shire, “Somali Remittance Companies and Their Clients,” p. 25.

73. Omer, *Supporting Systems and Procedures for the Effective Regulation and Monitoring of Somali Remittance Companies (Hawala)*, p. 21. For example, by one estimate each U.S. dollar remitted to Mexico raised the Mexican gross national product by \$2.69–3.17. Kulaksiz and Perdekova, “Somali Remittance Sector,” p. 7. For information regarding Somalia, see Ismail I. Ahmed, “Remittances and Their Economic Impact in Post-War Somaliland,” *Disasters* 24, no. 4 (December 2000): 386.

74. Hammond et al., *Cash and Compassion*, p. 49 (citing UN OCHA figure).

75. Personal interview no. 27.

76. Survey response no. 12.

77. Survey response no. 11.

78. Survey response no. 8.

79. U.S. Central Intelligence Agency, “Somalia,” *World Factbook*, 8 February 2012, <https://www.cia.gov/library/publications/the-world-factbook/geos/so.html>.

80. World Bank, *Somalia: From Resilience Towards Recovery and Development*, 34356-SO, 2005, p. 14, http://siteresources.worldbank.org/INTSOMALIA/Resources/cem_01_06.pdf.

81. Waldo, “Somalia Remittances,” p. 20.

82. Hammond et al., *Cash and Compassion*, pp. 3, 41.

83. Omer, *Supporting Systems and Procedures for the Effective Regulation and Monitoring of Somali Remittance Companies (Hawala)*, p. 15.

84. See UN Development Programme (UNDP) and World Bank, “Socio-Economic Survey 2002: Somalia,” *Somalia Watching Brief Report*, no. 1 (2003), http://siteresources.worldbank.org/INTSOMALIA/Resources/swb_complete_report.pdf (estimating remittances to Somalia at \$365 million).

regulatory official noted, there is “endemic misclassification of funds and transactions even when formally reported” in this sector.⁸⁵

How Do Remittances Move?

Somali remittances are largely understood by regulators and at times in the academic literature as a kind of charitable or migrant wage pipeline to Somalia. They do serve this role, but that pipeline is only one part of a much larger, networked machine in which these financial flows are transformed into highly profitable currency swaps and trade financing mechanisms that straddle the informal and

formal global financial systems. Like much of the global financial system, the margins involved in some of these transactions are very small, but the volumes of funds moving are so large that net profits are substantial.

Understanding this system requires a careful tracking of how money moves within it and an analysis of the resulting business niches and business models. This section focuses on how value moves through the system, and in the next section, this report explores how value is variously extracted, giving rise to different business models at different points in the network. Box 1 summarizes the process, which is explained at more length below.

The basic arrangement involves a collector, called an agent, who receives value from a client.⁸⁶ In charitable and retail

BOX 1. HOW DOES MONEY MOVE TO AND FROM SOMALIA?

AGENT/COLLECTOR – The basic arrangement involves a collector (“agent”) who receives value, usually in the form of cash from a client. The agent is often physically located in a small kiosk inside an Internet café, mobile telephone service center, or foreign exchange bureau somewhere accessible to a Somali migrant community.

“INFORMATION TRANSFER” and **“VALUE TRANSFER”** – Remittances follow a three-step process. First, the sending agent communicates information instructing the paying-out agent, either directly or through one or more intermediaries, to make the payment in the stated amount to the intended recipient. This usually occurs very quickly (less than 24 hours later) via telephone, radio, SMS, e-mail, or instant messaging. Second, the sending agent will receive and

consolidate several remittances at the send point before depositing these amounts into a bank account, possibly through a “head agent,” at some point organizing a bulk value transfer to a central bank account affiliated with the central processing unit or clearinghouse of the company or group, often in Dubai. Some time may elapse between these steps. Third, at some point the various agents in the network will settle any debts between them resulting from the first and second steps. This may happen through bilateral or frequently multilateral settlement. It often involves the transfer of value from the clearinghouse to the paying-out point, in many cases involving trade financing mechanisms.

TRADE STREAM – Value is transmitted from the clearinghouse to the paying-out point through trade transactions. The clearinghouse, usually in Dubai, will sell value previously remitted by the sending agents to traders, who use those funds to settle purchasing contracts, often in foreign currencies, especially U.S. dollars. These traders will then sell their goods in East Africa and use the resulting funds to pay the paying agent in local currencies or U.S. dollars for the currency they purchased from the clearinghouse.

PAYING-OUT AGENT – The agent on the other side of the transaction provides the recipient of funds with payment. Payments are cash or trade based.

See further Figures 1a and 1b on page 20.

85. Personal interview no. 15.

86. The account that follows is based on personal interview nos. 1, 3–7, 9–12, 14, 16–22, 25, and 27 and survey response nos. 1–3, 8, 9, and 11–13. See Shire, “Somali Remittance Companies and Their Clients.”

situations, this is frequently cash handed over in person by a roving agent or at a fixed storefront location, often a small kiosk inside an Internet café, mobile telephone service center, or foreign exchange bureau somewhere accessible to a Somali migrant community. Sometimes these collections are made at a mosque. When the SRO moves from a pure charitable basis toward a retail or commercial model, agents will be employed, often part-time or on a commission basis,⁸⁷ working under a franchise agreement with a head agent for that area or country. The head agent will require the subagent to provide a security deposit as a form of insurance against the subagent's malfeasance. The head agent's role is to consolidate retail transactions within a particular region of the country, access economies of scale and provide centralized functions such as monitoring and relaying exchange rates, and manage bank accounts.⁸⁸ This model is prevalent everywhere there are Somali diaspora communities: East Africa, the United States, the United Kingdom, Europe, and increasingly Asia.⁸⁹

The transactions involve an information transfer and a value transfer. The information transfer involves the sending agent somehow instructing the paying-out agent directly or through one or more intermediaries to make the payment in the stated amount to the intended recipient. A central processing unit, frequently based in Dubai, sometimes in Eastleigh or another regional center, is responsible for organizing, sorting, and filtering this information. This usually includes complying with international AML/CFT provisions, for example, by running the name of the remitter against international sanctions lists and blacklists using specialized software. The central clearinghouse then instructs the local paying-out agent in Somalia, Eastleigh, or wherever the transaction has been directed to pay the remittance. The local paying-out agent contacts the recipient to notify them that their remittance has arrived. The agent collects information from the recipient and verifies his or her identity, sometimes with the help of a trusted clan elder; the presentation of a

government-issued ID, which could be forged, may be less important than answering questions about one's clan or lineage relations based on information provided by the sender as security against fraud.⁹⁰ The agent then pays out the remittance to the recipient from the paying-out agent's account or cash reserve. The nominated recipient then frequently distributes that remittance to other beneficiaries in a manner that has been previously agreed with the remitter. The paying-out agent lastly informs all the parties that the payment has been completed, and all parties update their records.

The transfer of value from sender to recipient happens within the space of 24 hours or often much faster⁹¹ even while no actual value has changed hands between the sending agent and the paying-out agent, i.e., debts have not yet been reconciled. SROs will use whatever method of communication is cost and time efficient and reliable: telephone, radio, SMS, e-mail, or instant messaging. This is one of the key strengths of the Somali business model because, unlike a formal bank, money can be paid out wherever the organization can find an agent they trust. That agent need not be on their own payroll; it may be someone "lent" by another organization under a commercial arrangement or simply someone who agrees to conduct the transaction on a one-off basis for a small fee. SROs can thus pay out cash in the most remote, conflict-, and drought-affected corners of Somalia—places that banks could never operate in a cost-effective manner.

At some later point, the various agents involved will process the value transfer. Usually, the sending agent will receive and consolidate several remittances at the send point before depositing these amounts into a bank account, possibly through a head agent, at some point organizing a bulk transfer to a central bank account affiliated with the central processing unit or clearinghouse of the company or group. Bulk transfers are typically sent via formal banking channels

87. Shire, "Somali Remittance Companies and Their Clients," pp. 26–27.

88. See Ballard, "Hawala Transformed," pp. 8–9.

89. Personal interview nos. 1 and 11.

90. Little, *Somalia*, pp. 142–143.

91. See Hamza, "Somali Remittance Sector in Canada," p. 6; Anna Lindley, *Somalia Country Study*, ESRC Centre on Migration, Policy and Society, 15 January 2005, p. 10, <http://www.dfid.gov.uk/R4D/PDF/Outputs/EC-PREP/InformalRemittanceSomaliaStudy.pdf>.

to accounts in Dubai;⁹² Djibouti;⁹³ in some cases, our interviews suggest, Sharjah; or Nairobi.⁹⁴ There is also some evidence that consolidation accounts are held in other major regional financial centers, such as New York and Hong Kong. One interviewee suggested that there was evidence of these settlements continuing to occur via cash courier from an OECD country to accounts in Dubai, although this appears to be becoming less frequent.⁹⁵

The commingling of funds in this way creates headaches for regulators because it obscures the source of the funds involved and reduces the chances of identifying “linked” transactions, but it is a crucial part of the business model. Waiting until the sending agent or his head agent accumulates a significant sum before transferring funds to a central processing unit or clearinghouse is part of the strategy that allows SROs to pass on lower transfer costs to the remitter; fewer wire transfers create savings across multiple smaller transactions. Moreover, the consolidation of funds creates economies of scale that allows SRO clearinghouses in Dubai to use those funds as backing against other transactions that require larger amounts of capital, such as import/export transactions and foreign exchange speculation.

The passage of the funds through a central clearinghouse, usually in Dubai, creates regulatory challenges. The movement of funds by formal channels to Dubai allows relatively good visibility of these transactions, but the movement from Dubai is frequently through more informal channels, often trade-based funds transfers.⁹⁶ This point seems to be only partially understood by some regulators. One survey response we received suggested that funds from Dubai are primarily “transported physically” to their final destination.⁹⁷

After the central clearinghouse has received funds from the sending agent or from multiple sending agents whose tranches have been consolidated, the central unit will contract with a regional trader to deposit money with the paying-out agent,⁹⁸ essentially an adaptation of the old franco valuta system. The trader will deposit a portion of his proceeds from selling imports into Somalia, Eastleigh, or Djibouti with local paying-out agents of the remittance organization. The trader will then be reimbursed by the central clearinghouse in the currency that the trader needs to pay his invoices, usually U.S. dollars for tax-free purchases in Dubai. The paying-out agent will keep safe the money in local currency to be used for paying further beneficiaries.⁹⁹

From a purely mechanical perspective, it does not matter whether the trade onto which clearinghouses in Dubai piggy-back their trade stream transactions is in licit goods such as foodstuffs, cars, textiles, and livestock; controlled or illegal substances (qaat); or illicit services such as human smuggling and trafficking, arms trafficking, and piracy.¹⁰⁰ All of these methods lend themselves to collocation and intertwining of larger commercial remittance concerns with import/export or trading companies, which indeed occurs in the major Somali trading hubs, especially Dubai, Eastleigh, and Djibouti. Other methods may be used for transferring value within the network, including under- or overstatement of trade value (under- or overinvoicing to transfer value) and outright smuggling (illegal exchange of goods).¹⁰¹ Our research suggests that the physical movement of cash is avoided wherever possible because it takes time, is insecure, and raises transaction costs.

92. Personal interview no. 14.

93. Lindley, *Somalia Country Study*, p. 11.

94. Personal interview nos. 1, 4, 5, 8, 11, 14–16, 18, 21, and 22.

95. Personal interview no. 14.

96. Rita O'Sullivan, “ADB’s AMLCFT Policy and Alternative Remittance Systems” (paper, ADB–IDB/MIF–UNDP Joint Conference on Remittances, Manila, 12–13 September 2005), p. 4, <http://www.apgml.org/frameworks/docs/8/AML-CFT-Policy-and-Alternative-Remittance-Systems.pdf>.

97. Survey response no. 9.

98. Personal interview nos. 16, 17, and 19; Lindley, “Between ‘Dirty Money’ and ‘Development Capital,’” p. 525.

99. Shire, “Somali Remittance Companies and Their Clients,” p. 27.

100. We also received some information suggesting that qaat and human smuggling to Somali communities in Europe are sources of remittance revenues and may be used to facilitate value transfers. Personal interview no. 27; survey response no. 9.

101. Matteo Vaccani, “Alternative Remittance Systems and Terrorism Financing: Issues in Risk Management.” *World Bank Working Paper*, no. 180 (2010), p. 5, http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/Alternative_Remittance_Systems.pdf.

Figure 1a. Bank Wire Stream

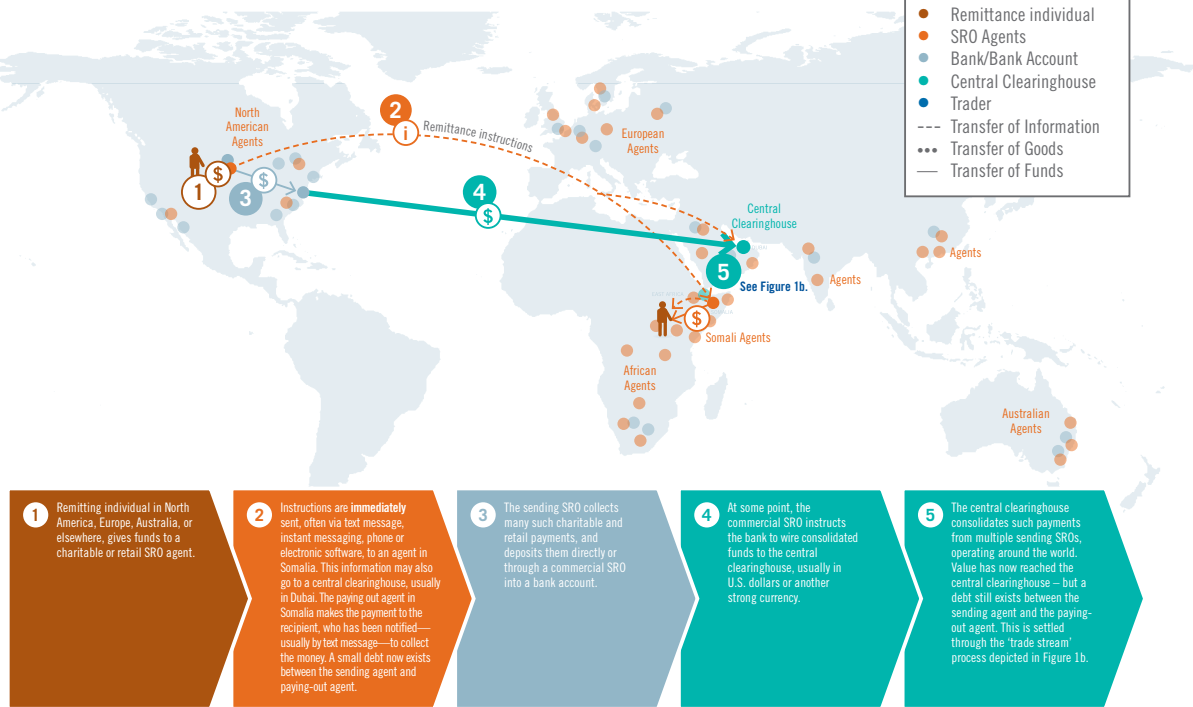
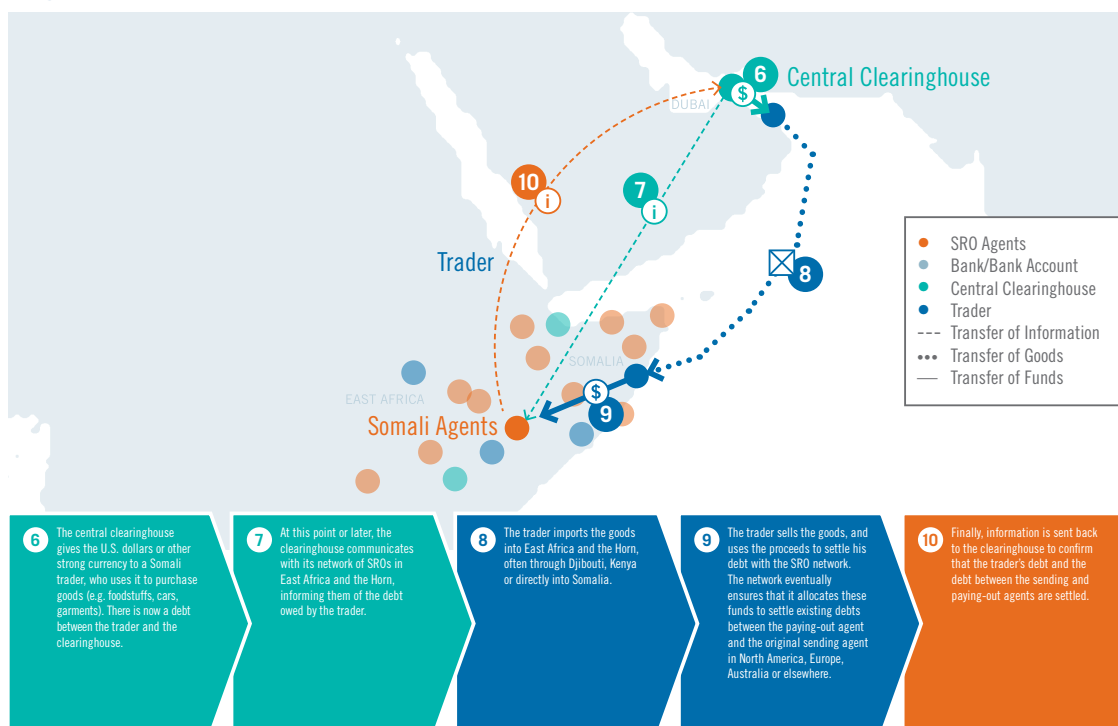


Figure 1b. Trade Stream



The resulting system is essentially a complex network of back-to-back currency swaps¹⁰² organized around two major streams, one constituting a “bank wire stream” swapping OECD currencies for U.S. dollars in the central hub, usually Dubai, and the other swapping those U.S. dollars for local currencies, often through trade-based transactions. Sometimes the second leg of this transaction does not in fact involve a swap. Payment out may be in U.S. dollars somewhere in East Africa, with the dollars moving from Dubai to East Africa through a trade-based mechanism or occasionally cash couriers (fig. 1).

Business Models

Although there is great fluidity in the organizational forms that SROs use, the system described above offers three basic opportunities to profit from participation—to monetize trust—through identifiably different although interrelated organizational types. At the outer ends of the network, charity and family networks collect and pay out remittances. Next, the retail SRO consolidates these funds, may interface with the formal financial sector through operation of a bank account, and moves funds from the outer extremity of the network to the center. Finally, commercial clearinghouses, often situated within foreign exchange houses or trading houses in Dubai, serve as a clearinghouse and switchboard and may leverage the large flows of remittances passing through them for currency speculation and trade financing purposes.

Even as this network forms a unified whole, each of these three different points within the network lends itself to different operational and ownership arrangements. Interestingly, our interviews also suggest that these types are seen in somewhat hierarchical terms. An SRO is seen as starting at the outer edges of the network and aspiring to make its way toward the center through organizational development over time. This section provides an overview of how these three types of business models work.

CHARITY AND FAMILY NETWORKS

Many remittance organizations appear to start out as informal charitable cooperatives, sending small amounts home to provide income support and charitable donations. One person, often drawn from within one extended family, clan, or lineage group, may emerge as the informal agent for the group, collecting periodic contributions; aggregating them, sometimes in a formal bank account; and organizing them for their remittance to a single recipient back in Somalia or in overseas Somali diaspora communities. That recipient may have separate instructions to distribute those consolidated funds to a variety of recipients within the extended family network in Somalia.

At this stage of their development, SROs frequently have little exposure to formal institutions and regulatory oversight. They have no physical storefront, and it may only be through opening a bank account or self-nomination that they come to the notice of state regulators. Frequently, a preexisting bank account is used, perhaps that of an existing NGO.¹⁰³ Women’s hagbad saving circles seem to play an important part in the use of this model in some communities.

RETAIL SROS

Over time, the agent may see the need to start charging charitable contributors a small fee to cover costs. It is only a small step from this arrangement to a retail remittance organization structure, where the agent assumes the role of soliciting remittances, consolidating them, and organizing them for payment out in Somalia or another Somali community. Such retail organizations may service the charitable niche within the Somali demand, but they may also actively encourage additional diaspora remittances, for example, to stimulate microenterprises or by way of investment.

Barriers to entry into this market are extremely low because the model relies heavily on existing social capital, mainly family and clan ties, to reduce the risks and operational costs of moving funds over large distances. These retail

102. Compare Roger Ballard, “The Operation of Hawala-Style Transjurisdictional Value Transfer Systems in the Contemporary Global Order: A Historical and Comparative Perspective,” n.d., pp. 32–34, <http://www.casas.org.uk/papers/pdfpapers/valuetransfers.pdf>.

103. Survey response nos. 2, 8, and 11.

startups are frequently privately owned corporations of one form or another with equity holders drawn from close-knit family groups, for example, a set of brothers or cousins. Owners are usually managers; one brother may be designated as the manager, or different brothers and cousins may manage the arms of the organization in different jurisdictions, often circulating to different outposts and back home to keep interpersonal family ties fresh and strong. Such retail SROs are frequently incubated within already existing family firms, allowing further costs savings through use of existing bookkeeping and telecommunications infrastructure, offices, and personnel and reduced advertising costs, as a preexisting Somali clientele already exists.¹⁰⁴ For that reason, a large proportion of such retail remittance organizations operate out of established Internet cafés, mobile phone retail kiosks, grocery stores, or even restaurants.¹⁰⁵

At this stage, remittance organizations may become more visible to regulators. As they grow, they are more likely to require a bank account and to be moving larger sums of money to reconcile debts internally or with other companies that will show up through existing supervision of the formal financial sector. Although advertising may well remain primarily word-of-mouth, they are more likely to acquire a storefront and perhaps begin advertising in local media. To grow within their local market, remitters may well engage additional agents as employees or contract staff to service parts of the community that are more difficult to reach.

Retail remittance organizations may retain their family-firm roots, but the need to maximize payment out options may lead to significant interfamily and cross-clan cooperation. Different retail organizations will work together on a commercial basis to allow payment out in as many places and as quickly as possible.

At the same time, dispersing different nodes of an SRO family network into different jurisdictions, subject to different regulatory stipulations, and working with different local client bases often leads them toward a decentralized ownership structure. Our research revealed a range of variations of multijurisdictional private firms structured in accordance with Islamic financial norms, none of them clearly dominant over the others:

- a parent company based in Dubai, likely sponsored for exchange purposes by a local businessman, with wholly owned subsidiaries operating in Europe, North America, and East Africa;
- a family of cobranded but autonomous companies with limited cross-ownership by a small group of brothers, held under a holding company based in the Dubai Free Zone;
- a head company with limited franchise agreements with a range of startups developed inside and outside the immediate subclan of the head company; and
- a highly vertically integrated multinational conglomerate based in Dubai, developing new service offerings in telecommunications and the financial sector to complement its core remittance business.¹⁰⁶

Still, legal form may not be an entirely accurate guide to influence and authority within these corporate groups. Our interviews suggested that senior males within these groups set strategy for the whole group, as in other hawala systems, but xawilaad hierarchies may be flatter than those of Arab hawala and Indian hundi networks,¹⁰⁷ given the traditionally highly democratic and meritocratic nature of Somali clan society, which places most adult males on a comparatively level footing, eschewing the inherited chieftaincy roles of many African societies.¹⁰⁸

104. Compare Thompson, *Trust Is the Coin of the Realm*, pp. 135–140 (discussion of the development of Indian *hundi* houses within Indian family firms).

105. Personal interview nos. 2 and 24; survey response nos. 8 and 12. See Saad A. Shire, “Transactions With Homeland: Remittance,” *Bildhaan* 4 (2004): 100–101; U.S. Department of the Treasury, “A Report to the Congress in Accordance With Section 359 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT ACT),” November 2002, p. 22, http://www.fincen.gov/news_room/rp/files/hawalarptfinal11222002.pdf.

106. Personal interview no. 16. Cross-ownership seems to be primarily by natural persons, not legal.

107. See Thompson, *Trust Is the Coin of the Realm*, p. 138.

108. Lewis, *Pastoral Democracy*, p. 114.

Retail remittance organizations make their profits through commissions on remittances and through exploitation of exchange rate spreads. Commissions are usually set around 3–4 percent of the funds remitted, 5 percent in some places for smaller retail transactions, and lower (1–2 percent) for charitable transactions. There appears to be remarkable parity in these rates across different local markets, regardless of the regulatory regime in place and the resulting administrative and compliance costs. These rates are uniformly lower than those charged by formal money transfer businesses such as MoneyGram and Western Union, which are usually 6–8 percent.

Commissions do not flow solely to the retail SRO. They are shared between the various agents or clearinghouses involved in any given transaction according to the terms of a predefined contract, sometimes within the franchise agreement between a retail SRO and the commercial clearinghouses. Our interviews suggest that a standard distribution of commissions would be 30–33 percent for the sending agent, 25 percent for the paying-out agent, and 42–45 percent for the holding or parent company typically based in Dubai.

Competition between retail SROs appears to be high, leading to very similar commission and cost structures. Our interviews suggested that these businesses operate on very thin margins, which is interesting for two reasons.

First, where regulation is perceived as being selectively applied, it is perceived as being discriminatory and unfair. By placing additional administrative costs on some firms and not others, it risks creating an unlevel playing field, to which those firms will respond by shirking their administrative responsibilities or engaging in ritualized compliance. Uniformity in regulatory implementation and enforcement therefore becomes central to its legitimacy as well as its effectiveness. As discussed in part 2, our research suggests that, for a variety of reasons, such uniformity in regulatory implementation is perceived by SROs to be lacking, not only across but within jurisdictions.

Second, despite their highly similar fee and cost structures, SROs do not seem to divide the market evenly. Some remittance organizations seem to have much larger market shares than others. Could delivery speed, customer care, or advertising explain this difference? The answer may actually be clan and family ties, which, in a close-to-perfectly competitive market, mediate consumer decisions by this proxy indicator of reliability.¹⁰⁹ We cannot prove this hypothesis with the data we gathered, although a simple customer survey in a multiclan market serviced by multiple SROs with different clan affiliations could certainly test it. If true, it suggests that clan and family ties have political and economic power that regulators would do well to heed or even harness. Part 3 discusses how regulators might go about that.

COMMERCIAL CLEARINGHOUSES

The key to understanding the SRO system may be the activity that occurs at the top level in the center of the network: the activities of the commercial clearinghouses. Much of the literature and many regulators tend to treat these entities as switchboards, directing transactions coming down one arm of the network to their intended destination. In some cases, other administrative functions, such as the role that these central hubs play in AML/CFT compliance arrangements or in operating consolidated bank accounts, are also noted. The key role played by these hubs, however, is often misunderstood.

First and foremost, these commercial clearinghouses are players in the global foreign exchange markets.¹¹⁰ The intertwining of SROs with foreign exchange markets and trade in this way is often reflected in the names of the organizations involved, many of which have “Forex” or “Trading” in the title. Seen from this perspective, SRO agents in sending states can be seen not as a mechanism for charity or for the fulfillment of traditional social obligations, but rather a huge network for sucking in large volumes of relatively strong, i.e., OECD, currencies that can easily be traded for U.S. dollars. These dollars are then swapped into large amounts of the weaker currencies in which payments are to

109. Personal interview nos. 14, 16, and 27; survey response no. 1; Hammond et al., *Cash and Compassion*, p. 56; Gundel, “Migration-Development Nexus,” p. 269.

110. See Ballard, “Hawala Transformed,” p. 26.

occur (e.g., Kenyan shillings, Somali shillings, or Djiboutian francs) either through another foreign exchange transaction or through a trade-based transaction that involves a purchase of U.S. dollars wherever the central SRO is located, for a payment out in local currency at the other end of the transaction. Importation of goods bought in U.S. dollars and sold in the local currency is a favored mechanism because importers frequently need to settle the accounts for their purchases in dollars. Through such import/export transactions, commercial clearinghouses underwrite the Somali import economy and appear frequently to get a piece of it. Healthy profits ensue for the middleman.

Seen from this systemic perspective, SROs are essentially brokers that solicit and consolidate huge number of retail deposits that are used against giant currency swaps: British pounds for U.S. dollars, U.S. dollars for Somali or Kenyan shillings. The key barrier for a retail SRO looking to break into this inner circle is primarily one of scale. Cross-border commercial ventures will be unwilling to include SROs in import transactions until they can be assured that the organization has sufficient “float”—access to sufficient cash—to settle their invoices wherever they are purchasing goods, frequently Dubai or Nairobi.¹¹¹ Once again, family and clan ties seem to play a significant role, serving as a kind of guarantee or as a ready-made social network from which SROs can raise capital and seek other forms of support. In some cases, however, capital-raising requirements may lead to cooperation across jilib or even clan lines. For example, Amal, the second-largest SRO after Dahabshiil, was formed in 1997 through the consolidation of 13 existing retail SROs, according to one interviewee.

The growth of an SRO from this point seems naturally to lead to increased institutionalization and professionalization. The close relationship between management and ownership may be diluted as the number of equity-holders is increased, although it seems typically to stay within the family or at least the clan. More sophisticated accountancy and communication infrastructures appear, together with an improved capacity to monitor and exploit exchange rate

movements and usually significantly greater investment in positive due diligence. Many SROs operating at this level will use transaction and exchange rate tracking software, often operating across multiple sites. In many cases, cost savings will be found by locating back-end operations in a central network hub, with other locations in the organizations’ network depending on it to conduct due diligence and bookkeeping clearinghouse functions.

Commercial clearinghouses frequently represent the apex of a set of pyramidal relations with other SROs drawn from a particular family or clan group. Their power to extract revenue from within this network is made clear by the fact that they take the lion’s share of commissions charged to remitting clients (42–45 percent). Yet, rarely do these central clearinghouses assume ownership of the agents operating on their behalf at the outer edges of the network. (Dahabshiil is the key exception here, with a much more centralized corporate structure, stretching across multiple jurisdictions.) Instead, most SRO networks appear to remain notably horizontal, based on a flat network structure.

Commercial clearinghouses necessarily do very substantial business outside their clan networks. They form partnerships across clan lines to maximize payment out coverage in Somalia and beyond.¹¹² They work with formal financial actors for similar reasons. Amal has an agreement with Wegagen Bank in Ethiopia that allows Amal to pay out through Wegagen’s network. Some SROs have relations with African Banking Corporation to pay in southern Africa. Dahabshiil has previously partnered with MoneyGram to conduct its business in parts of Somalia. In addition, SROs may move into other markets. Dahabshiil is a major investor in hospitals and medical infrastructure;¹¹³ Amal is similarly positioned in construction, especially shopping centers; and many of these clearinghouses have taken positions related to importing fuel, water, textiles, and construction materials into Somalia.

111. Personal interview no. 1.

112. Lindley, *Early Morning Phone Call*, p. 38.

113. Guled, “UN Refugee Agency Launches Inaugural Somali Community Event in Kenya.”

SRO Geography: Streams and Hubs

The public perception of Somali remittances is that they flow almost downhill from senders in OECD states to recipients in Somalia in a kind of direct current. Certainly, there is a redistribution of capital in this direction, but the reality is more complex on at least three levels. First, not all remittances handled through SROs flow to Somalia. They are directed to Egypt, Ethiopia, Kenya, South Sudan, Sudan, the UAE, Yemen, and even China and other countries where the Somali diaspora lives and works, according to several interviewees.¹¹⁴ Second, the transfer of value is not direct but passed down an SRO network through a series of carefully calibrated interlocking transactions that involve financial and trade exchanges running into and out of Somalia. Third, the flow of value rarely runs directly to Somalia. Instead, it takes a much more circuitous route, often passing through key “locks,” or hubs, where the financial power of consolidated remittances can be leveraged to underwrite some kind of other transaction, usually a foreign exchange or import/export transaction.

The result is that SROs have a very specific geography (fig. 1). At least two specific streams are identifiable. The first involves the redistribution of capital by migrant workers in OECD countries sending money home, through SROs making use of bank wire channels – so we call it the “bank wire stream.” This stream does not flow to Somalia, however, but to Dubai or in some cases to another hub near Somalia, such as Eastleigh or Djibouti. The hubs serve as a lock or switch, interfacing between the bank wire stream and what we might call a trade stream, built off the back of the traditional bazaar, the transnational money markets that conducted credit transfers for wholesale and forward trade

in Asian and Middle Eastern economies and which continue to fall between “superimposed European capitalism” and indigenous and local subsistence economies in that part of the world.¹¹⁵ This trade stream uses trade finance transactions as the vehicle for the transfer of value from Dubai to its final destination in East Africa.

Hubs such as Dubai and Eastleigh play a key role in regulating the flows within these streams.¹¹⁶ There, Somali businessmen are conducting their duty-free import/export businesses and require access to foreign exchange, which SRO clearing-houses can offer.¹¹⁷ It is no accident that these “switching” functions occur in those places because in part the regulatory arrangements in each place allow SROs to play these functions. Enterprises registered as Free Zone Enterprises in Dubai are left largely undisturbed by the UAE Central Bank as part of the UAE’s larger commercial strategy.¹¹⁸ Similarly, the Kenyan government leaves Eastleigh’s thriving Somali business community relatively undisturbed. In both cases, this facilitates SROs’ ability to construct foreign exchange swaps straddling the formal/informal divide.

It is also no accident that the ends of the pipelines through which remittances pass after they “disappear,” as many regulators described it to us,¹¹⁹ in Dubai or Eastleigh can often be found in war-affected economies (e.g., in Afghanistan and Somalia). Goods and services can pass from Dubai to places like those unimpeded by border control and official financial controls. It is also where other methods of transferring payments are not available. Even when other options exist, the comparative advantage of a hub or switch such as Dubai lies partly in moving value to these places faster and with less cost and hassle than if they were moved solely through formal channels. In turn, these war economies become key nodes in informal networks that pass value and goods to neighboring and regional countries.

114. Hamza, “Somali Remittance Sector in Canada,” p. 3.

115. Thompson, *Trust Is the Coin of the Realm*, pp. 128–135; Rajat Kanta Ray, “Asian Capital in the Age of European Domination: The Rise of the Bazaar, 1800–1914,” *Modern Asian Studies* 29, no. 3 (July 1995): 449–554.

116. On Dubai’s role in hawala transactions into Afghanistan, see Thompson, *Trust Is the Coin of the Realm*, pp. 200–204.

117. Ballard, “Hawala Transformed,” pp. 16–17; Monetary and Financial Systems Department, International Monetary Fund (IMF), *Approaches to a Regulatory Framework for Formal and Informal Remittance Systems: Experiences and Lessons*, 17 February 2005, <http://www.imf.org/external/np/pp/eng/2005/021705.pdf>.

118. Personal interview nos. 4, 8, 9, and 19.

119. Personal interview nos. 14 and 27.

This helps explain the strange phenomenon that is Eastleigh, a thriving, sophisticated, but almost completely informal Somali business enclave sitting within a suburb of Nairobi, Kenya's capital.¹²⁰ The space between Eastleigh and Kismayo plays the same role for the rest of the regional economies, as a trading hub for informal/formal exchanges and smuggling activities, as Afghanistan plays for Pakistan.¹²¹ A number of those we interviewed pointed to trading relationships between Eastleigh and other parts of East Africa, Yemen, and southern Africa as the basis for the circulation of currency used in remittance payments in Eastleigh and into Somalia. One interview subject, explaining the role of Somali trucking companies operating in southern Africa, including Tanzania and Zambia, related that their purchases of fuel in Somalia and Kenya for their own use and for smuggling and grey market resale in southern Africa, where government taxes are higher, are an important source of local hard currency for his remittance company. His SRO then allows them to repatriate their illicit profits to Nairobi or even Somalia.

Other interview subjects suggested that Eastleigh is increasingly taking on a role of clearinghouse for U.S. dollars similar to the role played by Dubai. They suggest that SROs operating in Puntland are couriering to Eastleigh the dollars that were deposited with them by piracy and human trafficking enterprises. They argued that although some of these dollars might be used for major purchases and investment in the region, including real estate and construction, many dollars were sold on the local black market. Others were simply rerouted back into other parts of Somalia where there was a shortage of dollars, given the dollarization occurring as a result of the rise of piracy and the presence of numerous international organizations.¹²²

Political Impacts: SRO Corridors

Our research suggests that, within these broad remittance and trade streams, it may be possible to identify specific remittance “corridors,” particular routes, whether physical or virtual, along which remittances habitually flow.¹²³ Of particular interest in the Somali context, because consumer choice in the SRO market appears to be mediated by clan affiliation, this suggests the possibility of identifying the contours of clan influence within the transnationalized Somali political economy. A map of SRO corridors thus offers the prospect of mapping preexisting trust networks and, in the process, of mapping the ripples of risk through these networks to the shores of the regulators that must deal with them.

Political and military groups clearly use SROs to actively solicit funds for their activities within Somalia, sometimes using traditional notions of diya to pressure diaspora members to make financial contributions.¹²⁴ Remittances are thought to increase prior to elections as political parties solicit support.¹²⁵ In some cases, SROs have clearly become a conduit for conflict financing, particularly where conflicts are protracted.¹²⁶ The UN Development Programme (UNDP) found that remittances increase in response to interclan warfare as a way to arm and finance militias.¹²⁷ One example identified by peacebuilding researcher Cindy Horst relates to a dispute between the Saleebaan and Sacad clans, which are both subclans of the Hawiye Habar Gidr clan, between 2004 and 2006.

The conflict was mainly financed by clan members from both clans in the diaspora. Every clan member

120. See Lindley, “Protracted Displacement and Remittances”; Little, *Somalia*, pp. 165–166.

121. Compare Ballard, “Hawala Transformed,” pp. 17–18. For information concerning Kismayo's role as a port of destination and disappearance for goods nominally bound for Mogadishu, see UN Security Council, *Letter Dated 18 July 2011 From the Chairman of the Security Council Committee Pursuant to Resolutions 751 (1992) and 1907 (2009) Concerning Somalia and Eritrea Addressed to the President of the Security Council*, S/2011/433, 18 July 2011, paras. 30–31, 72–75 (hereinafter 2011 Somalia and Eritrea monitoring group report).

122. Personal interview nos. 16 and 18.

123. Vaccani, “Alternative Remittance Systems and Terrorism Financing,” p. 15.

124. Hammond et al., *Cash and Compassion*, p. 77.

125. *Ibid.*

126. Horst, “Transnational Political Engagements of Refugees,” pp. 330–331; Horst and Gaas, *Remittances for Peace?*, pp. 17–18; Anna Lindley, “Migration and Financial Transfers: UK–Somalia,” *Refugee* 23, no. 2 (Summer 2006): 22.

127. Gundel, “Migration-Development Nexus,” p. 271.

in Norway was expected to contribute a specific amount and monthly sums of US\$300 per person were not uncommon. The money was collected by a committee and sent to the respective clan. In Somalia, each clan had assigned an individual for receiving these funds. This *khasnaji* (treasurer) was responsible for distributing the funds to the *mooryaan* (young fighters), who were fighting on behalf of his clan and for buying ammunitions. A key informant indicates that US\$200,000 was sent from Norway to both clans between the start and end of the conflict.¹²⁸

Horst claims that, at the lowest subclan levels, “US\$500,000 could easily be collected through diaspora contributions, whereas at clan level, such contributions could reach up to US\$5 million during the course of a single conflict.”¹²⁹ At this scale, remittances inevitably have an impact on the survival, shadow, and war economies of Somalia because as in other places where they have been more closely studied, such as Afghanistan, the networks that constitute each of these economies are intertwined.¹³⁰

Still, remittances here simply respond to social dynamics on the ground. They do not seem to be a driver of conflict onset, although they may sustain it. It would be wrong to assume that if SROs fund political activity, it is inevitably negative, competitive, or conflict fueling. In fact, recent research suggests that the Somali diaspora also uses SROs to fund peace talks.¹³¹ Examples include

- the 2003 Puntland Peace Agreement between the Habr Je’elo subclan of the Isaaq and the Warsangeli subclan of the Harti, underwritten by the diaspora

agreeing to fund exceptionally high diya payments (\$10,000 base rate, plus 100 camels, plus burial expenses, plus 40 million Somali shillings [\$25,000] in family compensation for each death);¹³²

- the 2004 Dharkeyn-Geenyo Peace Agreement, resolving disputes within the Dhulbahante over grazing rights, division of territory between Puntland and Somaliland, revenge killings, and the qaat trade;
- the 2005 Ramada Peace Agreement between the Reer Mahad and the Reer Khalaf clans of the Majerteen; and
- the 2006 Mahas Peace Agreement between the Hawadle and Murasade clans of the Saleeman and the Habr Gedir subclans of the Hawiye.¹³³

The same point can be seen in considering the relationship between remittances and taxation. At one level, the strength of private remittance networks seems to be a threat to the state because clan-oriented SROs reduce tax revenues and state control of imports¹³⁴ and provide an ongoing source of external financing fueling the centrifugal forces within the country. The activities of SROs may lead to an underinvestment in public goods by the state, reinforcing the tendency for the state to be seen as a prize for private capture. Continued contributions of the diaspora to basic services such as education and social services may embed attitudes of social neglect in government allocations.¹³⁵ In the northern regions of Puntland and Somaliland, for example, most government spending goes to security and general administration, with minimal investment in infrastructure and social services.¹³⁶ Throughout the country, education services are highly dependent on diaspora contributions,¹³⁷ and remittances now sustain private sector provision of other public services

128. Horst, “Transnational Political Engagements of Refugees,” pp. 330–331.

129. *Ibid.*, p. 331.

130. See Jonathan Goodhand, “Frontiers and Wars: The Opium Economy in Afghanistan,” *Journal of Agrarian Change* 5, no. 2 (April 2005).

131. Hammond et al., *Cash and Compassion*, p. 76. Compare Ahmed, “Remittances and Their Economic Impact in Post-War Somaliland,” p. 386.

132. Hammond et al., *Cash and Compassion*, p. 81.

133. *Ibid.*, pp. 80–81.

134. Marie Chêne, “Hawala Remittance Laundering System and Money,” *U4 Expert Answer*, 23 May 2008, <http://www.u4.no/helpdesk/helpdesk/query.cfm?id=170>.

135. Lindley, “Influence of Migration, Remittances, and Diaspora Donations on Education in Somali Society,” p. 17.

136. Kulaksiz and Purdekova, “Somali Remittance Sector,” p. 6.

137. Lindley, “Influence of Migration, Remittances, and Diaspora Donations on Education in Somali Society,” p. 15; Horst and Gaas, *Remittances for Peace?* p. 21; Markus Virgil Hoehne, “Diasporic Engagement in the Educational Sector in Post-Conflict Somaliland: A Contribution to Peacebuilding?” *Diaspora Working Paper*, no. 5 (August 2010), p. 10, http://www.diaspeace.org/D12_Hoehne_MPI.pdf.

in Somaliland, including electricity, garbage collection, and telephone services.¹³⁸

Although such an approach produces payoffs in the short term, it does little for long-term state building. It makes the whole system vulnerable to capture by private interests, including al-Shabaab;¹³⁹ piracy;¹⁴⁰ and grand corruption,¹⁴¹ as well as to extortion by force of arms. Tax receipts extracted from remittance organizations may well fuel the fragmentation of governmental authority in the country,¹⁴² perhaps even its Balkanization. It is suspected that profits from the remittance business helped al-Itihad and the Islamic Courts Union gain power and influence,¹⁴³ and regulators repeatedly voiced off-the-record concerns about al-Shabaab's ability to tax remittances.¹⁴⁴ Al-Shabaab's economic base is built on control of a range of trades, many of which rely on SROs for their cross-border activities.¹⁴⁵ It also appears that kinship plays a central role for those who do support al-Shabaab financially,¹⁴⁶ so SROs close to clan groups supporting al-Shabaab at any given time may be most at risk of capture by such interests.

On the other hand, however, peace-loving local authorities can use remittances to oppose such groups and reinforce governmental authority. For example, the nascent administration of Galmudug, controlled by the Sacad subclan of the Hawiye Habr Gadir, which has taken important steps against piracy and al-Shabaab forces, appears to be especially dependent on diaspora contributions.¹⁴⁷

Mapping Somali remittance corridors holds out the prospect of identifying how and where funds are flowing but not necessarily of predicting how they will be used once they arrive. It offers a way to map risk, not outcomes. If developed through further research, such a map or matrix identifying which clans send money through which international corridors might offer a more precise analysis of where there is a heightened risk at any given time of remittances supporting conflict, human rights abuse, or terrorism. That would serve regulators and remitters well because it would allow them to work together to cost-effectively address those risks, for example, by clarifying which specific corridors require heightened attention from regulators and on which Politically Exposed Persons (PEPs), SROs, and banks should focus their due diligence efforts. It would help reduce the costs and increase the effectiveness of AML/CFT efforts and human rights due diligence efforts required by the new UN Guiding Principles on Business and Human Rights. To be successful, any such effort will require regulators to understand not only how SROs work now but how they are likely to work in the near future.

138. Hamza, "Somali Remittance Sector in Canada," p. 37.

139. See 2011 Somalia and Eritrea monitoring group report, paras. 304–305, 322–325, 417, and 419; UN Security Council, *Letter Dated 10 March 2010 From the Chairman of the Security Council Committee Pursuant to Resolutions 751 (1992) and 1907 (2009) Concerning Somalia and Eritrea Addressed to the President of the Security Council*, S/2010/91, 10 March 2010, para. 93 (hereinafter 2010 Somalia monitoring group report); UN Security Council, *Letter Dated 10 December 2008 From the Chairman of the Security Council Committee Established Pursuant to Resolution 751 (1992) Concerning Somalia Addressed to the President of the Security Council*, S/2008/769, 10 December 2008, paras. 115, 212–215, and 231–234 (hereinafter 2008 Somalia monitoring group report).

140. Financial Action Task Force (FATF), *Organised Maritime Piracy and Related Kidnapping for Ransom*, July 2011, pp. 10 and 21, <http://www.oecd.org/dataoecd/40/13/48426561.pdf>; 2011 Somalia and Eritrea monitoring group report, paras. 87–121.

141. Charles Goredema, "Combating Illicit Financial Flows and Related Corruption in Africa: Towards a More Integrated and Effective Approach," *U4*, issue, no. 12 (October 2011), pp. 1, 12, and 16, <http://www.cmi.no/publications/file/4214-combating-illicit-financial-flows-and-related.pdf>.

142. Horst, "Transnational Political Engagements of Refugees," p. 329.

143. Andre Le Sage, "Prospects for Al Itihad and Islamist Radicalism in Somalia," *Review of African Political Economy* 27, no. 89 (September 2001): 475–476; Horst and Gaas, *Remittances for Peace?* pp. 15–16.

144. 2011 Somalia and Eritrea monitoring group report, para. 63.

145. *Ibid.*, paras. 60–80.

146. Valter Vilkkko, "Al-Shabaab: From External Support to Internal Extraction," March 2011, http://www.pcr.uu.se/digitalAssets/57/57537_MFS_paper_Vilkkko.pdf.

147. Hammond et al., *Cash and Compassion*, p. 76.

Looking Ahead

SROs have proven themselves highly adaptable to technological and social change. As we think about how to improve regulation of Somali remittances in the years ahead, we will need to consider not only how Somali remittances are organized now but how they are likely to respond to numerous sources of change in the years ahead, in particular the arrival of mobile phone-based financial services in Somalia and the arrival of formalized financial service providers.

MOBILE MONEY

African mobile communications markets are the most dynamic in the world. The African mobile market recently became the second-largest in the world after Asia, as ranked by the number of mobile devices.¹⁴⁸ The low purchasing power of the population using these devices has forced unparalleled innovation, particularly in such areas as mobile agriculture, mobile health, and especially mobile money. Mobile phones essentially offer unbanked Africans a direct link to the state and to family and commercial networks within their country and beyond. They are allowing African consumers to leapfrog traditional routes of integration into the global economy, which poses huge challenges for regulators and established market players such as banks. Where do SROs fit in?

The development of SROs within Somalia is closely related to the penetration of communications technology. The two industries have been symbiotic, and many SROs have helped establish Somalia's commercial phone companies.¹⁴⁹ Furthermore, the quality of telecommunications service greatly affects the volume of remittances that a household

will receive.¹⁵⁰ After telephone service was introduced widely in Hargeisa, remittances to that city tripled.¹⁵¹

Unsurprisingly, Somalia has been quick to adopt mobile money services, building on the strides in neighboring Kenya. Three years after Kenya's Safaricom launched m-Pesa in 2007, there were 18,000 m-Pesa agents, compared to 491 formal bank branches. More than 50 percent of adult Kenyans had signed up for m-Pesa, and it now accounts for more than 58 percent of electronic payments in Kenya.¹⁵² By no means do they have a monopoly. Others offering similar services in this market include Orange, AirTel, and Yu. One study claimed that the volume of transactions processed by m-Pesa in 2010 exceeded the volume processed globally by Western Union.¹⁵³ Eight and a half million users used m-Pesa to pay for goods and services, transfer money to other account holders, or simply hold value in a more secure form than cash. Similar services allow users access to a range of public and private disbursements and insurance systems, such as state pensions, life and agricultural insurance, health insurance, and microfinance loans.¹⁵⁴ These services have already reached Somalia. One SRO, Qaran, has partnered with Telesom/Harmuud to deliver ZAAD, a mobile money venture; Golis Telecom offers SAHAL; and Dahabshiil is offering some similar services through Somtel.

Some regulators we surveyed seemed to think that, in time, mobile money might displace more traditional xawilaad arrangements.¹⁵⁵ Perhaps unsurprisingly, the remitters characterize mobile money as being complementary to their existing service offerings rather than in direct competition. They emphasize that Somalia remains a cash-based society, so there still needs to be a system for transforming the money sent by mobile device into cash—a payment-out system,

148. AfricaFocus, "Africa: Fast-Paced Mobile Growth Continues," *AfricaFocus Bulletin*, 16 November 2011, <http://www.africafocus.org/docs11/ict1111.php>.

149. Ahmed, "Remittances and Their Economic Impact in Post-War Somaliland," p. 386; Lindley, *Somalia Country Study*, p. 12.

150. Gundel, "Migration-Development Nexus," p. 272.

151. Ahmed, "Remittances and Their Economic Impact in Post-War Somaliland," p. 386.

152. Michael Klein and Colin Mayer, "Mobile Banking and Financial Inclusion: The Regulatory Lessons," *World Bank Policy Research Working Paper*, no. 5664 (May 2011), p. 4.

153. *Ibid.*

154. Ignacio Mas and Dan Radcliffe, "Mobile Payments Go Viral: M-PESA in Kenya," March 2010, p. 5, http://siteresources.worldbank.org/AFRICAEXT/Resources/258643-1271798012256/M-PESA_Kenya.pdf.

155. Survey response no. 8.

which SRO networks can provide.¹⁵⁶ Mobile money services, such as ZAAD, ultimately rely on consumers' access to cash. In some cases, they point out, they may have positive development potential by allowing small-denomination transactions that SROs cannot arrange. With Somalia being an increasingly dollarized economy and very few U.S. coins circulating in Somalia, mobile money services allow small traders to charge mere cents, through payments into their mobile accounts, despite the absence of physical currency.

SROs see purely online money transfer options, such as WorldRemit,¹⁵⁷ as likely to achieve little market penetration, given the state of literacy and Internet access in the country. They also note that few mobile money arrangements provide for transnational money transfers outside the largest remittance corridors, and they suggest that telecoms companies are likely to face major bureaucratic challenges in getting formal approval for such arrangements from OECD regulators. If that is true, digitization may favor SROs and other informal money transfer businesses over more formal operators.

Mobile devices address the information transfer rather than value transfer portion of the process. They do not necessarily make it easier to move value around the world, although telecoms carriers, with their established infrastructures for managing direct client relationships and huge volumes of data, have an obvious affinity to the multilateral debt settlement process that underpins the SRO system.

Our research suggests there is a major opening for regulators to work together with SROs and telecommunications carriers to strengthen the relations between them. At the same time, such partnerships offer major payoffs for regulators because the digitized nature of mobile money offers greatly enhanced possibilities for automated data capture, reporting, risk assessment, and analysis.¹⁵⁸ Regulators will need, however, to overcome SRO cautiousness over hacking concerns.¹⁵⁹ In

addition, challenges remain in applying KYC rules to such systems because they are applied currently to the person who owns the account or SIM card rather than the person who actually receives the benefit of the money transferred to that account or SIM card.¹⁶⁰

Also, seizing this opportunity would place Somali and foreign state regulators in a position of serious advantage vis-à-vis local militant groups, who lack the technical expertise and financial wherewithal needed to exploit these technological openings. It is no accident that al-Shabaab imposed a ban on ZAAD in 2011;¹⁶¹ the mobile money venture threatened its ability to extort and control SROs operating in territory it controlled.

FORMAL FINANCIAL SERVICES AND SOMALI RECONSTRUCTION

Shifts in social, political, and regulatory circumstances on the ground in Somalia seem likely to challenge SROs in the months and years ahead. Already, Somaliland has permitted formal money transfer businesses such as MoneyGram and Western Union to operate there. What impact will this have on SROs?

At the charitable and retail end of the market, the impact seems likely to be minimal. Formal money transfer businesses find matching the cost structures of SROs difficult because SROs distribute compliance costs throughout a huge network. They also cannot match SRO reach into Somalia for small payments. Yet, they may have a bigger impact on the commercial end of the market. Formal money transfer businesses offer commercial clients security in the form of access to significant capital reserves, financial products that SROs may not offer and that banks do not offer in Somalia because they are not present in Somalia, and the implicit approval of Western regulators. All are likely to be particularly

156. Personal interview nos. 16 and 20.

157. Emmanuel Okoegwale, "WorldRemit Founder Wins Entrepreneurship Award for New Money Transfer System," *MobileMoneyAfrica*, 14 December 2010, <http://mobilemoneyafrica.com/worldremit-founder-wins-entrepreneurship-award-for-new-money-transfer-system/>.

158. Klein and Mayer, "Mobile Banking and Financial Inclusion," pp. 24–28.

159. Personal interview nos. 7 and 12.

160. Klein and Mayer, "Mobile Banking and Financial Inclusion," p. 13.

161. Personal interview no. 22.

attractive to major foreign investors seeking to move funds into, around, and out of Somalia. The real question is whether these formal money transfer businesses can begin to capture part of the Somali import/export finance market, particularly for the East Africa-Dubai corridor. If they do make inroads, the SRO model may come under serious pressure as SROs will find it more difficult to secure the local currency floats they need to guarantee payments out in East Africa.

SROs can adopt a strategy to mitigate this threat: preemption. Some anecdotal evidence suggests that SROs may begin to offer more complex financial products to Somali clients and consumers, occupying the space that formal money transfer businesses and, in time, foreign banks might fill. Some of the larger SROs now offer simple checking and savings accounts as well as foreign exchange services,¹⁶² and some now issue a rudimentary checkbook (a negotiable instrument) that can be used to withdraw money from other branch locations.¹⁶³ Dahabshiil, frequently a first-mover, has even opened its own bank in Djibouti.

How will SROs fit into or perhaps even drive the financial reconstruction of Somalia? SROs hold enormous power in the Somali political economy. They are the arteries for the financial lifeblood that keeps the Somali body politic alive through war and famine, drought, and tsunami despite being thinly stretched around the globe. They carry Somali identity and commerce to the farthest reaches of the globe and back again and are one of the most important sites of habitual interclan cooperation. It would be foolish not to harness the social capital that is embedded within these trust networks as a central component in the reconstruction of Somalia. Part 3 explores how that might be achieved and offers that increased trust will be required between regulators and remitters. To understand why that trust is currently lacking and how it might be generated, we examine how Somali remittances are regulated.

162. KPMG East Africa, *Feasibility Study on Financial Services in Somalia*, p. 69.

163. Lindley, "Between 'Dirty Money' and 'Development Capital,'" p. 534.

2. How Are Somali Remittances Regulated?

WHY REGULATE SOMALI REMITTANCES? A range of answers seem possible, as they would be for the regulation of any financial product or service: to protect consumers from the risk of fraud or monetary loss; to protect the market from accumulated risk and instability; to achieve broader macroeconomic objectives, such as regulating the supply of foreign exchange; to maximize revenues to the state; to maximize the development impact of the service; or to minimize risks of money laundering and terrorist financing.

The last objective has shaped international efforts over the last decade to regulate SROs. Ten of 14 responding FIUs cited AML/CFT issues as an objective of regulation. Other possible responses included consumer protection, with three jurisdictions choosing it as an objective of regulation; prudential/market stability (a choice of two jurisdictions); and the provision of accessible financial services (a choice for one jurisdiction). Development/overseas aid and national security received no mentions at all.

Concerns about SROs' vulnerability to terrorist financing clearly remain highly prominent in regulators' minds, fueled by

recurring and credible intelligence such as that presented by the UN monitoring team that oversees the implementation of UN Security Council sanctions on Somalia and Eritrea, revealing that al-Shabaab and the Eritrean government use the xawilaad network in their fundraising activities and terrorist operations.¹⁶⁴ Al-Shabaab proselytization and recruitment of diaspora youth in the last three years has raised concerns among host states that Somali youth may be becoming more generally radicalized, casting a broader shadow on remittances generally. In October 2008, Shirwa Ahmed became the first American suicide bomber in an attack in Bosasso. In December 2009, a member of the Danish-Somali diaspora attacked a medical school graduation ceremony at the Hotel Shamo in Mogadishu. In September 2010, Danish-Somalis attacked the Mogadishu airport in a suicide operation; and in May 2011, a member of the American-Somali diaspora attacked soldiers of the African Union Mission in Somalia in Mogadishu. There are ongoing concerns about the role of SROs in organized crime, especially piracy, in the Horn region,¹⁶⁵ and recent U.S. prosecutions allege that U.S.-based SROs were involved in transferring funds to al-Shabaab.¹⁶⁶ The regulation of Somali remittances in these jurisdictions takes place against this background of a heightened perception of risk.

164. 2011 Somalia and Eritrea monitoring group report, paras. 304–305, 322–325, 417, and 419; 2010 Somalia monitoring group report, para. 93; 2008 Somalia monitoring group report, paras. 115, 212–215, and 231–234.

165. Survey response no. 9; personal interview nos. 14, 24, and 27. See Shima Keene, "Hawala and Related Informal Value Transfer Systems: An Assessment in the Context of Organised Crime and Terrorist Finance," *Defence Academy Journal*, December 2007, http://www.da.mod.uk/journal/journal-downloads/defac_journal_hawala.pdf/view.

166. *United States of America v. Mohamud Abdi Yusuf, et al.*, 4:10-cr-00547-HEA-TIA (E.D. Mo., 2010), paras. 34–52; *United States of America v. Amina Farah Ali and Hawo Mohamed Hassan*, CR-10-187-PJS/FLN (Minn., 2011).

This part of the study explores how states and the international community regulate SROs to deal with these perceived risks. Our research identifies evidence of regulatory fragmentation or even confusion at the national level, with security agencies seeing SROs as representing a level of risk that is not matched by the resources that other responsible agencies devote to SRO regulation. Instead, responsibility for regulation tends to fall to prudential and financial system regulators, which often see regulation of SROs as a subset of a larger set of issues around remittances and alternative payment systems, and a relatively insignificant one at that. (One country responding to our survey of FIUs, for example, suggested that only 191 of 2,745 money transmitters registered in that country appears to have Somali links.¹⁶⁷) SROs themselves tend to experience regulation as somewhat fickle and arbitrary and question whether regulation is proportionate to the risk mitigation objectives that regulators espouse. The challenge is complicated by the significant cultural, linguistic, and social gaps that exist between staff in regulatory bodies, especially in OECD countries, and the actors within the SRO ecosystem. The result is a pervasive sense of distrust among OECD state regulators and SROs and sometimes perverse results in the implementation of the AML/CFT regime.

The central policy question with which this part grapples is maximizing the prospects of regulators achieving their regulatory objectives, given limited resources. There is a need to get beyond simplistic technical fixes such as registration and licensing and to begin to find ways to build partnerships between regulators and remitters. That will require a deeper understanding of how existing regulatory regimes work in practice and where Western bureaucratic traditions do and do not interface effectively with the trust networks within the SRO ecosystem. We should not assume that the best approach to regulation is formalization, pure and simple. Instead, we need first to better understand how SROs work in practice and then to look for opportunities to harness existing social capital within these trust networks toward our

regulatory objectives.¹⁶⁸ That may require a mix of formalization and professionalization by SROs and adaptation of working methods by regulators.

With regard to methodology, this study is not intended to provide a detailed description or cross-jurisdictional comparison of regulatory regimes around the world. Such analysis is available elsewhere.¹⁶⁹ Instead, our aim was to understand the perspectives of different stakeholders on how these regimes operate in practice and in particular to identify recurring themes across multiple jurisdictions. We pursued this goal through a combination of desk research, limited regulator interviews, and an online questionnaire shared with FIUs, to which we received 14 responses. The questionnaire itself can be found in appendix 2, with the list of respondents in appendix 1.

Self-Regulated Trust Networks

It is frequently said that because xawilaad and hawala networks are informal, they are unregulated. The Canadian Broadcasting Corporation, for example, states very simply that “hawalas are unregulated international financing networks.”¹⁷⁰ This is true if and only if we mean unregulated “by the state” or other external regulators.

SROs keep recordkeeping to a minimum, helping them keep administrative costs and overheads down and provide a lower-cost service than more formal institutions. SRO records only account for settlement between the sending and paying-out agents. Accounts for the network as a whole are not necessarily accessible by every agent or arm of the network in a comprehensive, integrated form. This arrangement helps reduce paperwork costs very significantly compared to more formal money transfer businesses and banks, where records at any point in the network are integrated with those of the rest of the network.¹⁷¹

167. Survey response no. 12.

168. For a related discussion, see Thompson, *Trust Is the Coin of the Realm*, pp. 63–67.

169. See IMF, *Approaches to a Regulatory Framework for Formal and Informal Remittance Systems*; Jonas Rusten Wang, “Regulating Hawala: A Comparison of Five National Approaches,” *Journal of Money Laundering Control* 14, no. 3 (2011).

170. “Money-Transfer Systems, Hawala Style,” *CBC News Online*, 11 June 2004, www.cbc.ca/news/background/banking/hawala.html.

171. Ballard, “Hawala Transformed,” pp. 6–8.

In truth, however, xawilaad systems are highly internally regulated, with the primary objective being risk reduction for the consumer. Any given SRO can rely on such minimal recordkeeping only because the costs of verification and transaction security are distributed efficiently across the entire network. Each node in the network monitors all the others, and if any SRO falls short of the performance standards expected of the whole network, for example, by failing to pay out the promised amount, that node will quickly be excluded from the network. The network is closed; the security of the network guarantees the security of each node. The higher overheads of formalized banking transfer systems partly reflect the fact that any bank may need to be able to settle with any other bank. It is an open system, so each node in the network must bear its own security costs, which cannot be decentralized and pooled as within a closed network.

The role of trust emerges again. In effect, SROs are capitalizing on trust. Specific forms of preexisting trust substitute for the capital that formalized money transfer businesses must sink into complicated bureaucratic systems of identity verification, capital reserves, and dedicated information and communications infrastructure. Any given hawaladar makes a profit because of his ability to participate in a transnational network of exchange. He can participate in that system because he is trusted. Each hawaladar can be described as “a specific local node of a huge self-regulating transnational network.”¹⁷² It is a “globally extended but comprehensively distributed system of self-regulating reciprocities ... whose system-security is grounded in the networks of absolute trust which hawaladars at all levels so carefully maintain as the very foundation of their business.”¹⁷³

Hawaladar and SRO guardedness against external regulators is thus not necessarily the result of “having something to hide” but is a fierce protection of the social capital on which their entire operating system is built. Seen from this perspective, a guardedness against external intervention, especially coming

from a quarter that is seen as not entirely sensitive to how the system operates, is comprehensible. The concern is that the introduction of excessive reporting requirements into the system will impede the low-cost, fast-delivery service model on which SROs operate and undermine trust within the network.

The key to hawala is that partners ... fulfil [*sic*] their obligations promptly and to the letter: all other considerations—with the exception of those which have a bearing on one’s partner’s reputation for trustworthiness—are regarded as entirely immaterial.¹⁷⁴

Yet, the problem for external regulators is that, unlike the SROs themselves, they might have to consider a number of other regulatory objectives, such as reduced money laundering and terrorism financing risk or reduced risk of financing human rights abuse. SROs may actually have such obligations, as the recent UN Guiding Principles on Business and Human Rights have made clear, but they may not yet appreciate that they have these obligations. The challenge for regulators is to find ways to encourage practices by SROs that pursue these regulatory objectives without undermining the SRO business model. It is a challenge with which they have struggled for the last decade.

A Decade of Distrust

Even before 9/11, there was a growing suspicion among regulators that hawalas and other remittance organizations were vulnerable to abuse for money laundering and terrorist financing purposes.¹⁷⁵ The basic and undeniable problem is that the structure of remittance transactions lends itself to layering and hiding the origin and destination of funds illicitly gained or maliciously intended.¹⁷⁶ Yet soon after

172. *Ibid.*, p. 7.

173. *Ibid.*

174. *Ibid.*, p. 12.

175. Nikos Passas, “Informal Value Transfer Systems and Criminal Organizations: A Study Into So-Called Underground Banking Networks,” Wetenschappelijk Onderzoek- en Documentatiecentrum, 14 December 1999, http://english.wodc.nl/images/on1999-4_Full%20text_tcm45-56889.pdf.

176. KPMG East Africa, *Feasibility Study on Financial Services in Somalia*, p. 27.

9/11, that suspicion seemed to harden into something of a premise, perhaps even a prejudice. The prevention of terrorism financing became the primary—some might say exclusive—focus of regulation, leading to a series of actions that generated deep and abiding distrust between SROs and regulators. This section briefly summarizes those efforts and the most important attempts that have been made in the last decade to overcome this gulf of distrust.

AL-BARAKAAT

In November 2001, U.S. government pressure led to the closure of the largest SRO in the world and Somalia's largest private employer: al-Barakaat (Blessings). The U.S. government believed that al-Barakaat was transferring funds to al-Qaida operatives and skimming other funds transfers to help finance the group and other Islamist extremists and that Osama bin Laden was a silent partner within the organization itself.¹⁷⁷ At the instigation of the United States, al-Barakaat was listed by the UN Security Council under Resolution 1267, requiring all states to take measures that essentially shut it down. In subsequent years, at least two individuals were detained at Guantánamo Bay partially on the basis of alleged participation in al-Barakaat activities.¹⁷⁸

Those measures proved highly controversial on two grounds: an arguably weak evidence base presented by the U.S. authorities for their determination that al-Barakaat supported terrorist activity and the major humanitarian impact of the resulting intervention.¹⁷⁹ Both Somali households and numerous aid agencies relied on al-Barakaat; it handled roughly half of all Somali remittances at the time. Close to 700 employees lost their jobs around the world.¹⁸⁰ Yet, the regulatory position of the U.S. government privileged the objective of countering terrorist finance over the

protection of the humanitarian and developmental benefits of the remittances al-Barakaat handled. In announcing the measures, President George W. Bush made his position clear: “Today, we are taking another step in our fight against evil,” he said. “By shutting these networks down, we interrupt the murderers’ work.”¹⁸¹

Other SROs, notably Dahabshiil, quickly took over al-Barakaat's market share, but the damage to relations between regulators and the Somali remittance community had been done. The intervention against al-Barakaat put SROs on notice that there were grave consequences to entanglement with criminal and terrorist actors and even to underinvestment in effective internal risk management, such as KYC procedures. Clearly, the Somali remittance community has made a major investment in such controls over the past decade, perhaps in part because after the closure of al-Barakaat, they knew that regulators meant business. Our interviews suggest, however, that even today, there is a lingering perception on the part of regulators that SROs are somehow engaging in ritualized compliance, doing the bare minimum to avoid regulatory controls while somehow hiding their more suspect business in Dubai, beyond the gaze of OECD-area regulators.¹⁸²

Even if the intervention against al-Barakaat made the seriousness of regulators' intent clear to SROs, it also created a climate of deep mutual suspicion, defensiveness, and even hostility between Somali remitters and regulators—and not only U.S. regulators because other states, especially OECD states, had participated in the intervention. Although the U.S. government and the United Nations have subsequently released additional information about the relationship they suspect existed between al-Qaida and al-Barakaat, the paucity of public information at the time and the jingoistic rhetoric

177. See UN Security Council Committee Pursuant to Resolutions 1267 (1999) and 1898 (2011) Concerning Al-Qaida and Associated Individuals and Entities (1267 Committee), “Narrative Summary of Reasons for Listing: QE.A.24.01. Al-Barakaat,” 23 February 2010, <http://www.un.org/sc/committees/1267/NSQE02401E.shtml>.

178. Andrei Scheinkman et al., “The Guantánamo Docket: Ilkham Turdbyavich Batayev,” *New York Times*, n.d., <http://projects.nytimes.com/guantanamo/detainees/84-ilkham-turdbyavich-batayev>; Andrei Scheinkman et al., “The Guantánamo Docket: Mohammed Sulaymon Barre,” *New York Times*, n.d., <http://projects.nytimes.com/guantanamo/detainees/567-mohammed-sulaymon-barre>.

179. Tim Golden, “5 Months After Sanctions Against Somali Company, Scant Proof of Qaeda Tie,” *New York Times*, 13 April 2002.

180. Donald G. McNeil Jr., “How Blocking Assets Erased a Wisp of Prosperity,” *New York Times*, 13 April 2002.

181. Kathleen Day, “U.S. Islamic Cash Outlets Investigated; ‘Hawalas’ Suspected in Terror Funding,” *Washington Post*, 7 November 2001.

182. Personal interview nos. 14, 16, 24, and 27.

used by Bush in announcing the measures gave rise to a sense among SROs that regulators simply did not understand their business model and were irremediably prejudiced against them.

Just as our interviews revealed continuing distrust of SROs by OECD regulators, so they revealed a lingering perception by SROs that no matter what they do, they cannot displace regulator prejudices. As one SRO officer said, “Even though you want to comply, you are treated as a drug dealer.”¹⁸³ SROs perceive their system as a self-regulated self-help mechanism. The al-Barakaat intervention risked having a whiff of the past about it, bringing back Somali memories of unsuccessful past efforts by imperialist, and not only Western, powers to prevent the global South from getting ahead.¹⁸⁴ Simply put, it created a deep and abiding legacy of distrust.

INTERNATIONAL EFFORTS: BETWEEN FORMALIZATION AND PARTNERSHIP

As problematic as the closure of al-Barakaat proved, one upside was the discussion it provoked, particularly at the international level, regarding regulation. How could the benefits of Somali remittances be maintained while risks were minimized?

The debate quickly coalesced around three different regulatory models: bans, registration, and licensing. In October 2001, the Financial Action Task Force (FATF) issued nine Special Recommendations intended to encourage financial institutions to take steps to protect against terrorist financing. In subsequent years, these Special Recommendations were endorsed by major international institutions, including the UN Security Council, World Bank, and International Monetary Fund (IMF), giving them the force of international standards that national regulators and private financial institutions must meet if they do not wish to be excluded, i.e., banned, from the formal global financial system. What was Special Recommendation VI (but has recently been folded into a reworked version of the Recommendations)

stipulated that all remittance systems, including agents, should be subject to licensing or registration and should comply with other FATF recommendations, including those regarding due diligence and recordkeeping.

Each country should take measures to ensure that persons or legal entities, including agents, that provide a service for the transmission of money or value, including transmission through an informal money or value transfer system or network, should be licensed or registered and subject to all the FATF Recommendations that apply to banks and non-bank financial institutions. Each country should ensure that persons or legal entities that carry out this service illegally are subject to administrative, civil or criminal sanctions.¹⁸⁵

FATF explains the regulatory rationale for this recommendation.

Money or value transfer systems have shown themselves vulnerable to misuse for money laundering and terrorist financing purposes. The objective of Special Recommendation VI is to increase the transparency of payment flows by ensuring that jurisdictions impose consistent anti-money laundering and counter-terrorist financing measures on all forms of money/value transfer systems, particularly those traditionally operating outside the conventional financial sector and not currently subject to the FATF Recommendations. This Recommendation and Interpretative Note underscore the need to bring all money or value transfer services, whether formal or informal, within the ambit of certain minimum legal and regulatory requirements in accordance with the relevant FATF Recommendations.

Much of the international discussion since the adoption of Special Recommendation VI has focused on how this recommendation should be implemented in practice and particularly how intrusive registration and licensing requirements should be.¹⁸⁶

183. Personal interview no. 11.

184. Compare Ballard, “Hawala Transformed,” pp. 13–14, 24; Thompson, *Trust Is the Coin of the Realm*, pp. 119–127.

185. See FATF, “FATF IX Special Recommendations,” February 2008, pp. 13–15, <http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf>.

At the international level, that discussion has played out through evolving FATF interpretations and actions that have tended to zero in more and more on focusing regulators and SRO compliance activities on the most risky parts of any given SRO's business,¹⁸⁷ as well as through other international discussions. Many of those other discussions have moved between two poles: formalization, in which external regulators push SROs to adopt practices that bring them ever closer to their formalized peers, and partnership, in which regulators and SROs work together to find mutually acceptable regulatory solutions.

In its initial form in October 2001, Special Recommendation VI seemed to some to back up the hard-line formalization approach represented by the al-Barakaat intervention. It seemed to suggest that SROs must come in to the formal sector or risk sanctions. Yet on closer inspection, the requirement was only that SROs and other remitters register or, alternatively, receive a license, leaving national regulators substantial discretion as to how intrusive a regulatory model they would adopt.

The UAE quickly began to promote a light-touch approach, based on a more reconciliatory tone toward remittance service providers. In 2002 the UAE Central Bank and the IMF worked together to convene the International Conference on Hawala, which produced the *Abu Dhabi Declaration on Hawala*, cautioning against heavy-handed regulation.¹⁸⁸ The Second International Hawala Conference in 2004 placed further emphasis on dialogue. In 2005 the IMF published a set of proceedings from that conference that emphasized the real question of "how to implement the international standards, which are to some extent aspirational, in ways that take account of local circumstances and can result in more effective oversight."¹⁸⁹

Around the same time, UNDP was also pushing a more reconciliatory approach. In December 2003, it brought together 14 SROs to launch the Somali Financial Services Association (SFSA), intended to promote cooperation, advocacy, and self-regulation¹⁹⁰ in part to overcome regulators' perceptions that the sector was inherently risky. That objective was reflected in a requirement that member companies appoint a compliance officer to ensure company implementation of KYC and AML obligations.¹⁹¹ Preempting later work by FATF, the SFSA advocated a risk-based approach to dealing with customer identification. Levels of risk would be based on the type of customer (e.g., individual, NGO, business, charity), volume of transactions, nature of funds utilized during the transaction, a name check against pertinent CFT databases, the destination of remittances, the relationship between the sender and recipient, and money laundering risks specific to the jurisdiction concerned.¹⁹² Each member company was encouraged to conduct an annual review of its AML compliance program to ensure its effectiveness.¹⁹³

The SFSA seems to have held great promise as a cooperative platform for improving the regulation of SROs. Unfortunately, it collapsed, and it is not entirely clear why. Some of our interview subjects suggested that it collapsed under the weight of interclan politics.¹⁹⁴ In late 2005, UNDP Somalia appears to have employed a relative of a senior figure in the SFSA close to one particular SRO, thereby causing a split within the SFSA, leading at least one major SRO (Dalsan) to defect. In July 2006, UNDP initiated a new program of capacity building and support for a new association formed in Dubai and London of those SROs that broke away from the SFSA, called the Somali Money Transmitters Association (SOMTA). This group included six SROs (Amal Express, Dahabshiil, Global Money Transfer, Mustaqbal, Qaran

186. FATF, *Risk-Based Approach: Guidance for Money Service Businesses*, July 2009, <http://www.fatf-gafi.org/dataoecd/45/1/43249256.pdf>; FATF, *Combating the Abuse of Alternative Remittance Systems: International Best Practices*, 20 June 2003, <http://www.fatf-gafi.org/dataoecd/39/17/34033713.pdf>.

187. See FATF, *Risk-Based Approach*.

188. IMF, *Approaches to a Regulatory Framework for Formal and Informal Remittance Systems*, pp. 94–95.

189. *Ibid.*, p. 3.

190. UNDP, "Somali Financial Services Association Launched," 4 December 2003, <http://mirror.undp.org/somalia/presssfs.htm>.

191. Somali Financial Services Association, "Anti-Money Laundering Compliance Guide," July 2004, p. 14, <http://mirror.undp.org/somalia/Remittance/SFSA%20Compliance%20Guide.pdf>.

192. *Ibid.*, pp. 19–21.

193. *Ibid.*, p. 48.

194. Personal interview nos. 1 and 16.

Express, and Sahan) that UNDP estimated as having a 75 percent market share.¹⁹⁵ This program was intended in part to help SROs implement their KYC and other AML/CFT obligations, including through the creation of a shared, Internet-based transaction tracking system that would have improved transparency for regulators while helping keep SRO costs down.¹⁹⁶

Yet by October 2006, the SRO community was submitting formal complaint letters to UNDP regarding allegations of corrupt dealings between UNDP Somalia and contractors working on the program. UNDP Somalia selected a U.S. company, PayQuik, to develop the online compliance software, and three years later, the software was finally delivered. None of our interview subjects now claim to use it, instead relying on alternatives sourced in the market, including World-Check. During 2007, the enterprise unraveled under the pressure of divisions within SRO ranks, intertwined with allegations of possible corruption in UNDP's administration of the program.¹⁹⁷ The whistleblower's allegations that some funds under the program were being directed to Islamist militants inside Somalia also probably spooked donors. No major partnership efforts have been undertaken since that time. SROs seem reluctant to engage in another such effort, given their mistrust of the international community as a result of this experience and their experiences with failed political and security interventions by the international community over the last two decades.

NATIONAL EFFORTS: PRAGMATIC CONVERGENCE?

Few countries are now interested in banning hawalas or SROs. Such an approach is seen in OECD countries as simply driving these practices "further underground."¹⁹⁸ Some East

African countries have bans on their books, but our interviews suggest that it is widely recognized that these bans are unenforceable. In fact, the situation in those countries seems to be closer to one of "don't ask, don't tell." For example, in Kenya only banks or remitters who partner with banks are officially licensed to carry out money transfers, yet SROs are clearly thriving and dealing with banks and foreign exchange houses.¹⁹⁹ SROs in Kenya currently exist in something of a grey zone, with obligations under the *Proceeds of Crime and AML Act* of 2009 but without access to a licensing or registration regime. Foreign exchange houses in Nairobi complain bitterly about the unlevel playing field that results,²⁰⁰ but officials seem willing to tolerate it, perhaps in part because SROs are a central source of U.S. dollars in Nairobi, operating through black market exchanges in Eastleigh and City Market. Those markets in turn feed the patronage machines on which many Kenyan politicians and officials rely.²⁰¹ Numerous other countries, including some OECD countries, that we contacted denied the presence of SROs in their territory, even though SRO owners and managers had themselves told us they operate in those countries.²⁰²

Instead, evidence suggests that many jurisdictions are slowly converging around a hybrid of the licensing and registration models.²⁰³ In both approaches, money transfer businesses are encouraged to formalize their role and required to meet certain KYC and suspicious transaction report (STR) obligations. The registration approach imposes lower, if any, standards of conduct, however, through a less intrusive application and ongoing inspection process and usually through lower deposit, capitalization, and directorial character/conduct (fit-and-proper) tests. Formally, states as diverse as Denmark, Italy, Uganda, and Yemen use a licensing

195. UNDP Somalia Information Office, "UNDP Somalia Quarterly Update," July 2006, <http://reliefweb.int/node/417089>.

196. For the text of the SOMTA memorandum of understanding, see <http://shimronletters.blogspot.com/2008/06/somali-money-transmitters-association.html>.

197. Mark Trevelyan, "Whistleblower Accuses UNDP Over Somalia Projects," Reuters, 16 May 2008.

198. Personal interview nos. 14, 23, and 24.

199. Personal interview nos. 16 and 18–21; Lindley, "Between 'Dirty Money' and 'Development Capital,'" p. 533.

200. Personal interview nos. 3 and 16.

201. Personal interview no. 18.

202. Personal interview no. 24; survey response no. 6.

203. See generally Rusten Wang, "Regulating Hawala."

system. Registration regimes formally exist in Somalia, the UAE,²⁰⁴ and the United Kingdom²⁰⁵ and at the federal level in the United States. At the U.S. state level, however, there is massive variation in regulatory arrangements, which is itself seen as causing major headaches by many SROs. Broadly speaking, the requirements that regulators are imposing seem to be steadily if slowly converging.

The United Kingdom, for example, started with a relatively light-touch registration approach in 2000 but moved to a more stringent approach after the adoption of the European Union's Payment Services Directive in 2007, introducing fit-and-proper tests and requiring money transfer businesses to apply for a new license from the UK Financial Services Authority (FSA) or, if they were sufficiently small, to have the license requirement waived. At the other end of the spectrum are jurisdictions such as Germany, the Netherlands, and Norway, which require transfer organizations to demonstrate a higher level of professional expertise and capitalization than under the UK approach. Penalties for violation of the regime are also higher (up to three years imprisonment in Germany).²⁰⁶ Norway has moved toward the center, deciding in 2010 to use the EU Payment Services Directive "waiver" option for most money transfer organizations, which facilitated registration of smaller money transfer organizations by, for example, relaxing capitalization requirements.²⁰⁷

There have been tentative but important signals from the Obama administration of a willingness to move in a similar direction. The U.S. Department of the Treasury and the U.S. Financial Crimes Enforcement Network have undertaken a number of outreach efforts to the Somali community

recently, including a webinar in December 2011 on AML/CFT issues. When it became clear that formal U.S.-based banking channels might become closed to SROs, the Treasury Department took a number of steps to reassure banks that their due diligence obligations in dealing with these organizations were manageable. The Treasury Department even went so far as to blog about the issue, stating that it was the "view of the Treasury Department that financial institutions that establish and maintain appropriate risk-based anti-money laundering programs will be well-positioned to appropriately manage such accounts, prevent illicit transactions, and avoid enforcement action."²⁰⁸

These shifts may reflect a growing realization by regulators that the regulatory regimes that impose excessive burdens on SROs may simply not have the intended results.²⁰⁹ Instead of drawing SROs toward the transparency produced by formalization, excessively burdensome licensing arrangements may push them in the opposite direction. As a recent Australian study found, "[M]any such businesses are unlikely to have the organizational skills necessary to implement the regulatory framework required."²¹⁰

Although some claim that registration and licensing efforts have led to high take-up rates by SROs,²¹¹ our research concludes that the story is more complex. First, we conclude that many SROs continue to operate "under the radar." Levels of formalization seem to be quite corridor specific. One study found, for example, higher levels of formalization in the UK-Somali corridor than the Dutch-Somali corridor;²¹² and that can probably be broken down further into subcorridors, possibly associated with specific clans and SRO groups. The UK government estimates, for example, that there are

204. Salah Eldin Eltayeb, "Central Bank Registers All Somali Remittance Agents," *Khaleej Times Online*, 25 June 2004, http://www.khaleejtimes.com/DisplayArticleNew.asp?section=business&xfile=data/business/2004/june/business_june464.xml.

205. William Vlcek, "Development vs. Terrorism: Money Transfers and EU Financial Regulations in the UK," *British Journal of Politics and International Relations* 10, no. 2 (May 2008): 293.

206. See FATF, *Mutual Evaluation Report: Anti-Money Laundering and Combating the Financing of Terrorism: Germany*, 19 February 2010, <http://www.fatf-gafi.org/dataoecd/44/19/44886008.pdf>; Rusten Wang, "Regulating Hawala," pp. 213–215.

207. Norwegian Ministry of Finance, "Forskrift om betalingsforetak," 1 July 2010, www.regjeringen.no/nb/dep/fin/dok/lover_regler/forskrifter/2010/forskrift-1-juli-2010-om-betalingsforeta.html?id=610770

208. Scott Rembrandt, "The Importance of Remittances Through Legal Channels to Somalia," *Treasury Notes*, 23 December 2011, <http://www.treasury.gov/connect/blog/Pages/Importance-of-Remittances-through-Legal-Channels-to-Somalia.aspx>.

209. Personal interview no. 24.

210. Rees, "Money Laundering and Terrorism Financing Risks Posed by Alternative Remittance in Australia," p. xiii.

211. Lindley, "Between 'Dirty Money' and 'Development Capital,'" p. 533.

perhaps 2,700–3,500 money service businesses (not just SROs) in the United Kingdom, with some 30,000 agents on the books.²¹³ Yet, currently only roughly 730 of these are licensed as required by UK law, with 400 applications in process, suggesting that some 1,500–2,500 have not sought the required license. Another OECD state suggested to us that the licensing system in their country catches only 5–10 percent of remittances.²¹⁴

This is highly counterproductive from a regulatory perspective, not least because it creates “false positives” for FIUs in those countries.

[T]he presence of unregistered [remittance organizations] will create a lot of “false positives” for the FIUs. Hawala operators sending large accumulated funds as regular bank transfers will attract suspicion and often trigger STRs. In effect, that means that the systems used to uncover money laundering will be “spammed” by legitimate migrant remittances. In addition to disturbing the investigation, this can also deter law enforcement agencies from taking action, since they fear targeting the financial lifeline of disadvantaged groups.²¹⁵

Second, we saw evidence suggesting that SROs move operations across borders to minimize the compliance costs imposed by different regulatory regimes.

[M]ost retail hawaladars in Europe, North America and the [Persian] Gulf have by now taken steps to ensure that their store-front operations conform to regulatory best practice; by contrast the system’s back-office procedures, most especially with regard to such issues as consolidation, settlement counter-flows and distribution remain as obscure as ever.²¹⁶

Some SROs told us that they have moved back-end operations, including KYC obligations, where possible, to the UAE from OECD countries because it is simply seen as “easier” to do business there, in terms of the regulatory environment being less intrusive and imposing less burdensome obligations.²¹⁷ Regulators suggested something similar is happening under the EU Payment Service Directive’s “passporting” provisions, which allow financial institutions licensed in one EU jurisdiction to carry on operations throughout the EU.²¹⁸

Overly onerous regulatory requirements may thus risk pushing some SROs, especially the smaller retail SROs, away from the formal sector, counterproductively reducing transparency.²¹⁹ One study explained the logic of an approach that provides a simplified regime for smaller SROs and hawala operators.

[T]he bulk of Hawala operators wish to run their business legally, as this will create many new opportunities and give greater security. If the threshold for licensing is put too high, however, many of these will lack the organizational and financial resources required to operate in the open. A simplified registration regime would therefore enable regulators to distinguish those who are willing to register from those who have something to hide.²²⁰

212. Rusten Wang, “Regulating Hawala,” pp. 216–217.

213. Personal interview nos. 1, 3, 23, and 24.

214. Personal interview no. 27.

215. Rusten Wang, “Regulating Hawala,” p. 221.

216. Ballard, “Hawala Transformed,” p. 23.

217. Personal interview nos. 4, 5, 7, and 10.

218. Personal interview nos. 14 and 24; survey response nos. 2 and 8. Compare Hammond et al., *Cash and Compassion*, p. 44.

219. Personal interview nos. 10, 14, 24, and 27; survey response no. 8.

220. Rusten Wang, “Regulating Hawala,” p. 221.

The challenge for regulators is to know just what burden different SROs will be able and willing to bear. As has been suggested throughout this study, that requires an improved understanding of how SROs operate, and it requires an improved understanding of how regulation interfaces with SROs.

Challenges in Implementation

Our interviews revealed a range of concerns on the part of SROs about how they were regulated. Most of these related to the imposition of administrative and compliance burdens that they found costly or disruptive to one degree or another or to a rationale that they did not understand. Examples included

- unclear timelines for processing license and registration applications,²²¹
- unresponsive regulators,²²²
- lack of access to Somali language materials and interpreters,
- disruptive and poorly explained inspection visits,²²³ and
- excessive fees and costs payable to regulators for the “honor” of being regulated.²²⁴

These obstacles to implementation are primarily caused by limited resources and limited attention to dialogue and engagement with SROs in a culturally sensitive manner. Regulators saw many of these expectations as unrealistic, given the limited resources regulators have available.²²⁵ The Swedish Finansinspektionen has publicly indicated that translation and interpretation costs needed for sufficient supervision would greatly exceed the fees paid by remitting organizations and cannot be justified.²²⁶ One obvious

remedy might be for regulators in multiple jurisdictions to pool costs, for example, by cofinancing the production of Somali language materials explaining basic regulatory requirements across multiple jurisdictions or cofinancing an Internet- or telephone-based inquiry line to respond to queries in Somali.

Box 2 lays out some of the key lessons for regulators identified through our research.

Two sets of recurring concerns raised repeatedly by SROs seem to go beyond the question of limited resources and limited outreach. Both relate to the challenges involved in grafting risk management systems designed for formal banks and other financial institutions operating in open markets onto SROs, which operate in closed trust networks. The first relates to KYC rules, and the second relates to STRs.

HOW DO YOU KNOW YOUR CUSTOMER?

The international regulatory regime set out in the FATF Special Recommendations and adapted through national laws requires SROs to take a series of steps to validate the identity of their customer and the source of funds being remitted and to ensure that they do not do business with customers known to be involved in money laundering or terrorist financing. These risk management protocols are designed to protect the entire financial system, and accordingly, the due diligence expected of SROs and other financial institutions grows with the potential risk involved in a particular transaction. As our interviewees attested, SROs have invested significant sums and effort over the last decade in building KYC systems into their operations. Most claimed to have AML/CFT training arrangements in place for all their agents and to run all transactions through a centralized KYC database, usually operated in Dubai, which

221. Personal interview nos. 16 and 17.

222. Personal interview no. 14, 16, and 24; survey response no. 2.

223. Interestingly, interview subjects praised Kenyan authorities for the way they handled such inspection visits, although these only occur for foreign exchange houses and not for SROs. Personal interview nos. 16, 18, 19, and 21.

224. Personal interview no. 21.

225. Personal interview no. 14.

226. Norwegian Financial Services Authority, “Reguleringen av pengeoverføringer fra Norge—en vurdering av muligheten for å gjøre pengeoverføring enklere, rimeligere, og lovlige,” 15 September 2008, p. 13, <http://www.hvitvasking.no/upload/Regulering%20av%20pengeoverf%C3%B8ringer%20fra%20Norge.pdf>.

BOX 2. 10 KEY LESSONS FOR REGULATORS

1. EXPLAIN SOMALI REMITTANCE ORGANIZATIONS (SROs) TO BANKS.

Banks play a key role in the SRO industry, as vehicles for wire transfers for accumulated remittance deposits and as proxy regulators for anti-money laundering/countering the financing of terrorism (AML/CFT) efforts. Yet, they often have a poor understanding of how SROs operate. Given their risk-averse culture, some banks will therefore choose not to do business with SROs, which can lead to adverse outcomes such as reductions in humanitarian assistance by diaspora communities. Regulators can help address this problem by working with SROs to undertake outreach to banks to better explain how the SRO industry operates.

2. PROVIDE ACCESS TO MATERIALS IN THE SOMALI LANGUAGE.

Disseminating materials to SROs to communicate compliance obligations in the Somali language can help reduce misunderstanding and mistrust and provide opportunities for improved engagement. Regulators should also consider sending Somali language translators on site inspection visits.

3. PROVIDE WRITTEN EXPLANATIONS OF REGULATORY DECISIONS.

Providing written, timely explanations of reasons for regulatory decisions such as the issuance or nonissuance of licenses, the results of inspection visits, and corrective measures that SROs can implement in their businesses will help create a regulatory partnership between regulators and SROs.

4. CALIBRATE REGULATORY FEES TO THE SIZE OF AN SRO.

Designing and implementing a scale of regulatory fees on the basis of the size of the SRO, either revenues or funds remitted, will help ensure that even the smallest charitable and retail SROs have a realistic chance to participate in the regulatory system and reduce incentives for them to operate underground.

5. OFFER GUIDANCE ON POLITICALLY EXPOSED PERSONS (PEPs) AND SUSPICIOUS TRANSACTION REPORTS (STRs).

It may be difficult to apply existing definitions of PEPs to the Somali context because there are multiple government institutions and family networks that may not map easily onto existing definitions. Working together with SROs to tailor reporting and due diligence guidelines to the Somali remittance context, and to ensure SROs are regularly providing the information that regulators need to help SROs identify PEPs, is a good way to align expectations between regulators and SROs and to strengthen regulatory cooperation.

6. BEWARE OF FALSE POSITIVES IN AML/CFT SOFTWARE.

Many Somali names are similar due to clan affiliation and genealogical linkages. The same name may also have multiple spellings in the Roman alphabet. Software-based due diligence systems inevitably raise numerous false positives, matching client names to those on a blacklist. Close attention by regulators is required to ensure this does not lead to incorrect punitive action.

7. ENCOURAGE TRADE ASSOCIATIONS. Trade associations can serve as a transmission belt conveying norms from government to industry and can help regulators to test and develop new norms and implementation arrangements. In addition, trade associations can help SROs implement their regulatory obligations by providing access to common

resources, such as implementation kits, training sessions, tailored software, and explanatory materials. Trade association groups may also offer a cost-effective way for regulators to engage SROs in dialogue.

8. FOSTER INFORMATION SHARING WITHIN GOVERNMENT.

Information about Somali remittances is often dispersed across multiple regulators within a given jurisdiction (police, intelligence services, development agencies, financial regulators, and immigration and multiculturalism services). Regular meetings to share this information, subject to legal restrictions, can help ensure that multiple regulatory objectives are met and the workings of SROs are better understood across government.

9. WORK WITH REGULATORS IN OTHER STATES.

Regulatory disparities between one state and its neighbors can create incentives for SROs to move their business to other jurisdictions. SROs are highly networked and can easily move operations to neighboring states. Passporting arrangements in EU states also allow some SROs to evade regulatory requirements, weakening the regulator's ability to ensure effective risk management in that jurisdiction. Regulators can address this through improved cross-border cooperation or even working toward regulatory harmonization.

10. BUILD THE CAPACITY OF REGULATORS IN EAST AFRICA.

The ability to ensure that AML/CFT and other regulatory objectives are met will be limited while regulation of SROs in East Africa remains as weak as it is now. States should work together to strengthen the capacity of regulators in East Africa.

ran the names involved in the remittance against all major international sanctions lists.

Yet, a number of problems have emerged along the way. First, regulators are concerned that some of the systems put in place are designed for show and that the systems do not address the heart of the problem: that an SRO operator does not necessarily know the origin of the money he is remitting or who its ultimate beneficiary will be. SROs routinely manifest all the indicators of compliance that regulators demand of them, and if regulators are not satisfied with those indicators, they should perhaps suspect their regulatory design rather than the SROs. Over the last decade, regulators have demanded that SROs exhibit these indicators, such as the nomination of a Money Laundering Reporting Officer, the conducting of AML/CFT training, or the use of a KYC database. Yet, they have offered little by way of capacity-building assistance to help SROs develop these capacities. As we saw in some cases, international actors such as UNDP have stepped in to try to offer some assistance. Inevitably, however, a market solution has emerged. A cottage industry of AML/CFT consultants has sprung up, some specializing in dealing with SROs. In many cases, they are highly professional; but in other cases, it seems questionable whether what is being produced is anything more than ritualized, outsourced compliance. One OECD country regulator found that numerous SROs were submitting applications prepared by the same individual, even with the same spelling mistakes.²²⁷ Such arrangements may achieve compliance with the regime regulators have imposed, but they probably do little to improve overall risk management. When asked about KYC requirements, most of our SRO interview subjects focused on going through ID checks with walk-in customers. Few had much to say about the application of enhanced due diligence to larger transactions to identify the source of revenues.²²⁸

Very few had anything to say about how KYC requirements should be applied at the payment-out end of the system, which reveals a second problem. Because of the structure of SRO chains, a sending agent's customer is only the original remitter, not the ultimate recipient of the remittance. Many recipients of remittances are receiving on behalf of other actors, reflected in the skew of remittances toward urban areas. Less than 5 percent of rural households receive remittances directly,²²⁹ but rural households as well as urban households rely on remittances. Therefore, someone must be passing them to others. One analyst claimed in 2002 that, in northern Somalia, 46 percent of urban households support relations in pastoralist areas.²³⁰ Even if an SRO in an OECD country meticulously discharges its KYC obligations, it will provide little transparency over the transaction once it passes through Dubai and into East Africa.²³¹

Arguably, the receiving or paying-out agent in East Africa or the central clearinghouse in Dubai will also be subject to KYC obligations and regulators in those countries will therefore have visibility over those parts of the transaction that OECD regulators do not. In practice, that does not happen. In Kenya, as we have seen, SROs operate outside the law, if not quite illegally, and outside the reach of regulators.²³² In Somalia, there is no effective regulator, and even in Dubai, the central bank's reach into the free trade zone is very limited. The problems in the operation of the AML/CFT regime in these places can thus not be fairly ascribed solely to SROs. They have as much at least to do with the way local regulatory authorities in those places interact with those remittance organizations.

Presently, regulators seem to rely primarily on SROs themselves to discharge these KYC obligations, but a third problem emerges, in that many SROs do not really see the rationale behind the KYC requirements. After all, thanks to the clan and jilib system on which SROs are built, SROs already

227. Personal interview no. 14.

228. Interview subjects engaged in foreign exchange trading seemed anecdotally to pay more attention to this issue. Personal interview nos. 20 and 25.

229. Ahmed, "Remittances and Their Economic Impact in Post-War Somaliland," p. 383.

230. Medani, "Financing Terrorism or Survival?" p. 4.

231. Jennifer Isern, Reni Deshpande, and Judith van Doorn, "Crafting a Money Transfers Strategy: Guidance for Pro-Poor Financial Service Providers," *CGAP Occasional Paper*, no. 10 (March 2005), <http://www.cgap.org/gm/document-1.9.2704/OP10.pdf>.

232. Personal interview no. 18.

know their customers and staff. One OECD country, for example, has encountered difficulties implementing a fit-and-proper test that requires SRO managers to have a certain number of months' experience in the industry because local community leaders argue that this is less important as an indicator of reliability than their own communities' trust in them.²³³ Similar problems emerge in relation to KYC rules. Simply by learning the customer's name, an SRO immediately has access to a customer's genealogy and to his extended, transnational family network. Somalis do not have separate given and family names, but a given name followed by their father's given name and then their grandfather's. As a result, many names are similar. Moreover, there is no uniform system of transliteration of Somali words into the Roman alphabet. One real world example illustrates the problem: the same person's name might be listed as Ali Mohamed Hashi, Maxamed Xaashi Cali, Mohamed Haashi Ali, and Mohamed Ali Haashi.²³⁴ Even the best KYC software struggles as a result, bringing up numerous false positives. One SRO complained that the software they used frequently matched client names to those on the blacklist published by the U.S. Office of Foreign Assets Control, suggesting that the person standing in front of them was "someone in an Iraqi prison or someone who is dead."²³⁵ Such a fallible system discourages those who must use it from anything but ritual compliance.

In the eyes of the SROs, the performance of such computerized verification systems compares poorly to their own social verification system, which reveals perhaps the central problem with the application of KYC rules in the SRO context. KYC rules are designed for application by banks and formalized financial institutions operating in the context of an open market. The customer is considered a stranger, entirely unknown to the bank or financial institution that must demand proof of identity in order to know the customer through 1) assuring itself that the customer is who she says she is and 2) undertaking due diligence to determine whether there is any reason the bank or financial institution should not deal with her –

for example because she has been placed on a UN or U.S. blacklist. Neither step maps comfortably onto the relationship between an SRO and its customer. SROs consider that the customer's clan or lineage membership, evident in their very name, makes them known at a very significant level to the organization. If you know their family, you have a guarantee of identity and an instant assessment of risk profile that may be more socially significant to Somalis than any government-issued ID. From the regulators' perspective, SRO reliance on family ties creates obvious concerns, particularly around potential conflicts of interest and the reluctance of remittance organizations to pass to regulators information they might acquire about potentially suspicious aspects of a particular remitter's activities. From the SRO perspective, KYC measures appear significantly redundant.

WHAT IS A SUSPICIOUS TRANSACTION?

Similar problems emerge around the application of suspicious transaction reporting or suspicious activity reporting by SROs. The FATF regime, adapted into national law, requires financial institutions to report suspicious transactions to regulators. Over the last decade, the cottage industry described above has helped SROs to build internal systems to identify such suspicious transactions, but the operation of those systems cannot be outsourced to external consultants because it involves the exercise of SRO staff discretion to determine when any given transaction may be suspicious. Again, the major problem is regulatory design.

Simply stated, what regulators and SROs see as suspicious is by no means identical.²³⁶ On the contrary, SROs "don't see much suspicious activity."²³⁷ As Ahmed al Qamzi, head of the UAE Central Bank's Anti-Money Laundering Unit stated bluntly, describing his expectations of reporting from hawala operators more generally, "We don't expect to receive any suspicious transaction reports from hawaladars. The system is built on trust."²³⁸

233. Personal interview no. 14.

234. 2011 Somalia and Eritrea monitoring group report, para. 323.

235. Personal interview no. 17.

236. Personal interview no. 16.

237. Personal interview no. 25.

238. Thompson, *Trust Is the Coin of the Realm*, p. 265.

The regime gives SROs little incentive to enquire into the sources of the funds they are handling. On the contrary, many of them see such enquiries as likely to be bad for business. As made brutally clear in one interview, a high street foreign exchange bureau manager in Nairobi who deals with SROs told the story of how he had asked a new customer about the source of a large amount of U.S. dollars. The customer explained that it had come from prostitution at a local hotel frequented by Westerners. The interview subject complained that he never saw this customer again, suggesting he saw it as evidence that compliance with AML norms cost him legitimate business or at least that Westerners' promotion of the norms that drove that business away was somehow hypocritical.²³⁹ Arguably, this case demonstrated that AML norms operated as intended, depriving an organizer of crime the opportunity to launder money through this particular channel.

Two further problems related to reporting suspicious transactions also emerged from our research. First, because SRO compliance arrangements are distributed across an SRO's entire network, with most SROs assigning sending agents responsibility for KYC obligations and head agents at the regional level responsibility for STR obligations, SROs rarely identify linked transactions, which have been broken into smaller parts to fall under the threshold at which enhanced KYC due diligence obligations may apply. As one state regulator acknowledged, "Money service businesses like Western Union basically have a mini FIU to deal with these things. It's just not realistic to expect the little guys to make that kind of investment."²⁴⁰

Second, because any given SRO agent's knowledge horizon is much closer than the end of the remittance transaction, SROs have little ability to identify systemic patterns, such as the emergence of heightened risk in a specific corridor. Any given SRO may not be aware that the remittance they are handling is destined for a particular location or particular recipients exhibiting heightened risk exposure, for example, because an armed conflict has just broken out or there is heightened risk of human rights harm. Interestingly, only

one regulator indicated that they have a system in place for drawing money transfer businesses' attention to corridors with heightened risk.²⁴¹ No regulator has an early-warning system in place designed to call SROs' attention to specific risk corridors with which they may be dealing, such as remittances by certain clans or to certain locations when armed conflict breaks out.

WHO IS A POLITICALLY EXPOSED PERSON IN SOMALIA?

SROs' limited capacity to discharge their STR obligations is particularly acute in the area of PEPs, who are treated by the international AML/CFT regime as having a heightened risk profile and therefore requiring particular attention by financial institutions. FATF defines PEPs as

individuals who are or have been entrusted with prominent public functions in a foreign country, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, [and] important political party officials. Business relationships with family members or close associates of PEPs involve reputational risks similar to those with PEPs themselves. The definition is not intended to cover middle ranking or more junior individuals in the foregoing categories.

How should this definition be applied to Somalia? First, is the president of Puntland a PEP, or the president of Somaliland? Neither rules a foreign country recognized in most jurisdictions, and so neither is likely to be covered by the definition of PEP that applies in most countries. The CIA World Leaders list, for example, does not include references to Puntland or Somaliland officials. Yet, surely both are just as politically exposed and thus just as vulnerable to AML/CFT risk as a member of the Transitional Federal Government of Somalia (TFG). Second, who is a "family member" for the purpose of this definition? In applying this provision, most states have adopted definitions of family members that restrict coverage to the nuclear family,

239. Personal interview no. 18.

240. Personal interview no. 24.

241. Personal interview no. 23.

i.e., spouses, parents, siblings, children, and spouse's parents or siblings. In the context of Somali families, however, that may not be the end of the story. Jilib and other subclan ties may exert a similarly powerful pull as those exerted by nuclear family members in Western settings.

SROs have received very little guidance from regulators on how to discharge their obligations in this area,²⁴² and perhaps even more remarkably, there is none freely available. The regime imposed by FATF has created a similar market dynamic in this area as it has in others, imposing a demand on SROs and other money transfer businesses without a matching supply of interpretive expertise. The market has stepped in to fill the gap, with numerous commercial risk management organizations now offering proprietary PEP lists for a handsome fee.

This approach seems highly counterproductive and entirely unnecessary. By imposing obligations on SROs without guidance on the content of those obligations, regulators have set up a situation that incentivizes ritual compliance and undermines the regime's central objective of risk management. How can SROs effectively manage risk if they do not know what they are supposed to be looking for? Many simply cannot afford to purchase the PEP lists offered to banks and large, formal money transfer businesses. Furthermore, this outcome is unnecessary because, as explored in part 3, there may be cost-effective ways in which regulators can work together to provide authoritative guidance to SROs on these questions at relatively low cost or even free of charge.

WHERE DO BANKS FIT IN?

Perhaps the biggest bottleneck in the current regulatory system exists around banks. Nearly every SRO interviewed identified their relationship with banks as one of the largest

problems they face.²⁴³ One directly declared, “[B]anks are the people who have really screwed up this business.”²⁴⁴

The problem again is regulatory design. Regulators give banks responsibility and discretion for deciding which clients are too risky for them to take on. As one money transmitter association official said, the regime “makes banks into informal regulators.” Because regulators have helped to fan perceptions that SROs are inherently risky, many banks see the costs involved with managing the risk they perceive of being associated with SROs as far outweighing the benefits of the business SROs bring in.²⁴⁵ Banks may undertake their own site visits and due diligence inquiries within SRO offices, replicating the work done by state regulators, but not passing their insights to the national regulator.²⁴⁶ They may increase fees for SROs to subsidize the cost of discharging these risk management tasks delegated to them by the state and to hedge against risks posed by SROs.²⁴⁷ Ultimately, they may refuse to do business with these organizations.²⁴⁸ In East Africa, only Barclay's Bank routinely agrees to do business with SROs.²⁴⁹ In the United Kingdom, Barclay's wrote to many money transfer businesses in late 2011 indicating that it would only deal with them if they acquired a license that, the national regulator told us, was intended only for larger businesses, not for smaller businesses such as many SROs. As a result, many SROs will likely lose access to Barclay's banking services because it will be too costly or difficult for them to acquire or maintain this license or they may simply not try. In the United States, in December 2011, the last bank dealing with SROs threatened to stop doing so following the conviction of two Somali women for terrorist financing through local SROs.²⁵⁰

This process of “debanking” is highly detrimental for SROs and those who rely on the remittances SROs move. SROs

242. Personal interview no. 24.

243. Personal interview no. 16.

244. Personal interview no. 18 (referring to the United Kingdom). A similar sentiment was expressed in personal interview nos. 10 and 11 in the UAE.

245. Personal interview nos. 14, 16, 24, and 27; survey response nos. 2 and 11–13.

246. Personal interview no. 3.

247. *Ibid.*

248. Shire, “Somali Remittance Companies and Their Clients,” pp. 29–30.

249. Personal interview nos. 3, 16, 17, and 25.

250. See Tran, “Aid Groups Lobby U.S. Not to Shut Off Remittances to Somalia.”

need banks, not so much to hold their money but rather to give them access to the formal wire transfer system that they use to conduct the inter-SRO settlements that underpin the SRO business model. Without access to that system or if it is too expensive, the entire business model is jeopardized. Yet, state regulators seem reluctant to intervene. As a U.S. Treasury Department blog post recently noted, national regulators generally do “not have the authority to direct any financial institution to open or maintain a particular account or relationship. The decision to maintain any financial relationship is made by each financial institution itself.”²⁵¹

The results are also perverse for other stakeholders, including the Somali nation, and regulators themselves. Because the Somali economy is so dependent on SROs for the full range of financial services, banks’ reluctance to do business with SROs is, as a recent study stated, “the single greatest threat to Somali private sector investment.”²⁵² That creates very strong incentives for SROs to find alternatives to the formal banking system to move value across borders and to turn to methods, such as overinvoicing on trade transactions, that regulators may find even more difficult to regulate.²⁵³ The result is a regime that produces the opposite of the intended result, and SROs go underground.

WHERE DO TRADE ASSOCIATIONS FIT IN?

When SROs confront common problems like this, it might be expected that they would form some common advocacy platform to advocate for regulatory reform.²⁵⁴ Our research suggests, however, that SROs have had a series of underwhelming experiences with such initiatives. This report has described how two internationally backed efforts to create a common advocacy platform for SROs—the SFSA and SOMTA—were brought low by a mixture of Somali clan politics and administrative incompetence. Our interviews suggest that SROs also do not feel well represented by

relevant trade associations that operate at the national level, whether they are Somali-specific, such as the Somali Business Association in the United Kingdom, or not, such as the UK Money Transmitters Association (UKMTA) and the Foreign Exchange and Remittance Group (FERG) in Dubai. SROs described themselves as feeling somewhat “disconnected” from these industry groups.²⁵⁵ SROs have a relatively small market share compared to others within these groups and therefore relatively weak influence over the policies and campaigns these groups adopt.²⁵⁶ Only one FERG member, for example, is explicitly recognized as having ties to SROs (al-Dahab Exchange, which deals with Dahabshiil).²⁵⁷

Nevertheless, we saw only limited evidence that SROs have made significant efforts to become enthusiastic participants in these trade association activities. Although it may not be realistic to expect SROs to “prove a negative,” as one remittance association official put it to us, and prove that their operations are not tainted by terrorism and money laundering, in fairness, SROs have not done everything that they could to explain their business model to banks and regulators. SROs seem largely content to deal with banks and regulators on a bilateral basis. They have not sought, for example, to work together to develop materials explaining to national regulators or FATF how the Somali remittance sector works or the massive humanitarian, development, and social benefits that Somali remittances offer Somalia.

In fact, some of the more significant efforts to foster SRO cooperation through trade associations seem to come from regulators rather than from SROs themselves. Some regulators see these trade associations as potentially playing an important role, serving as something of a transmission belt, conveying norms from government to industry and helping industry to implement its obligations. The United Kingdom has shown particular commitment to this model. For example, the support of the Department for International Development

251. Rembrandt, “Importance of Remittances Through Legal Channels to Somalia.”

252. Hammond et al., *Cash and Compassion*, p. 44.

253. Personal interview no. 19.

254. Personal interview no. 6.

255. Personal interview nos. 16, 17, 18.

256. Personal interview no. 16.

257. Personal interview no. 4.

and Her Majesty's Revenue and Customs (HMRC) for the UKMTA allowed smaller and midsize remittance organizations, such as retail SROs, to access that trade association.²⁵⁸ The HMRC continues to work with the UKMTA and other bodies, including the Joint Money-Laundering Steering Group, to give money service businesses a voice in regulatory processes and to produce useful and relevant training and educational materials.²⁵⁹

At this point, the full potential of these relationships may not have been canvassed in the SRO context. Trade association-style groups may offer a cost-efficient way for regulators to engage SROs in dialogue, joint activities, training, and the communication of risk warnings, but it may not be efficient or sustainable to form a separate group in each jurisdiction. Instead, as set out in part 3, it may be more attractive to have regulators work together to encourage SROs to join a multi-stakeholder process at the international level.

Regulatory Confusion?

The clear picture that emerged from our research is that SROs perceive the regulatory burden imposed by current approaches, whether framed as registration or licensing, as disproportionate to the risks involved in their business.²⁶⁰ As one interviewee said, "What do you get from a license? A headache."²⁶¹ The same interview subject later complained that he spent 80 percent of his time on compliance issues and said, "Compliance is killing the business."²⁶²

Undoubtedly, SROs and regulators view the risks associated with the SRO business differently. A large part of the problem seems to be the failure by regulators to convince SROs of the utility and importance of managing these risks by framing a coherent narrative presenting regulation as in the SROs' interest and to communicate that message consistently across government and different jurisdictions. One reason for this may be that regulatory strategies and responsibilities are fragmented across different government agencies, leading to a mismatch between statements on the risk involved in SRO business and the resources that government devotes to managing this risk. Few governments have an effective whole-of-government strategy framing common regulatory objectives in dealing with SROs.²⁶³

Different agencies within the same government seem to be pursuing different regulatory objectives. Ten of 14 FIUs responding to our online questionnaire cited AML/CFT issues as an objective of regulation. At the same time, none of them cited national security as an objective, even though numerous security agencies clearly see the intertwining of SROs, al-Shabaab, and Somali diaspora populations as a potential threat to their own country as well as to Somalia.²⁶⁴ None of our responding jurisdictions cited development concerns as an objective of regulation, but a number of jurisdictions have promoted the development benefits of remittances in recent years. Governments in Germany, the Netherlands, Norway, and the United Kingdom have developed websites designed to encourage transparency in the remittance market, thereby maximizing development benefits, by allowing consumers in their country to compare remittance prices.²⁶⁵ (One question that might be asked is why four websites were necessary and whether combining forces to produce one multilingual site marketed across all four jurisdictions might not have produced improved

258. Rusten Wang, "Regulating Hawala," p. 212.

259. FATF, *Third Mutual Evaluation Report: Anti-Money Laundering and Combating the Financing of Terrorism. The United Kingdom of Great Britain and Northern Ireland*, 29 June 2007, p. 200, <http://www.fatf-gafi.org/dataoecd/55/29/39064399.pdf>.

260. Personal interview no. 2.

261. Personal interview no. 3.

262. *Ibid.*

263. Both the United Kingdom and Canada, however, seem to be taking steps in this direction.

264. Personal interview no. 27. See UK Serious Organised Crime Agency, "The United Kingdom Threat Assessment of Organized Crime," 2009/10, p. 10, http://www.soca.gov.uk/about-soca/library/doc_download/54-the-united-kingdom-threat-assessment-of-organised-crime.pdf.

265. For the United Kingdom, see <http://www.fxcompared.com>. For the Netherlands, see <http://www.geldnaarhuis.nl>. For Norway, see <http://www.sendepengerhjem.no>. For Germany, see <http://www.geldtransferfair.de>.

market transparency. This need for coordinated and joint action across jurisdictions is addressed in part 3.)

This regulatory confusion is having real impacts in Somalia. Humanitarian assistance to Somalia during the terrible drought of the last year has been chilled by the uncertainty that NGOs face regarding whether and how they can move funds into Somalia, particularly those areas controlled by al-Shabaab.²⁶⁶ Concerns were heightened after the UN monitoring team for Somalia alleged that up to half of all World Food Programme aid to Somalia was being siphoned off, some of it to Islamist militants.²⁶⁷ For obvious reasons, humanitarian assistance actors tend to rely on the most liquid remitters to move funds into war zones, who may be liquid precisely because they access illicit or grey market funds.²⁶⁸ As a result, assistance providers may be providing funds to the very SROs that are most likely to be targeted for exploitation by local authorities, including al-Shabaab in some areas. It remains unclear whether SROs and humanitarian NGOs will be regulated with the maximization of humanitarian assistance as the primary regulatory objective or whether AML/CFT considerations will continue to trump all other regulatory objectives, leaving them vulnerable to prosecution.

Western regulators do not take the same approach to this issue elsewhere. In Afghanistan, regulators have largely overlooked the reliance of international actors on hawaladars despite clear knowledge that those same hawaladars are deeply involved in the financial aspects of Afghanistan's drug trade.²⁶⁹ Western states turning a blind eye to such practices in Afghanistan, where it apparently serves their interests to do so, but clamping down on Somali remittances leaves many in the SRO community feeling unfairly targeted.

It reinforces perceptions of regulation as arbitrary and disproportionate and reproduces an atmosphere of distrust.

There are other unintended outcomes of the currently fragmented approach to regulation at the national and international levels. Security agencies' perceptions of the high risks involved in the SRO business are matched neither by the perspectives of other agencies in their own governments nor by resources allocated by those agencies to this issue. For many of those other agencies, resources are allocated according to a very different risk metric, such as prudential risk and consumer protection, against which SROs seem comparatively unrisky.²⁷⁰

Against the legacy of the al-Barakaat intervention, the mismatch between the rhetoric of risk and the limited resources financial regulators devote to working with SROs leaves those SROs feeling highly vulnerable and confused. One interview subject stated that regulation in his host state was "so confusing that even the regulators don't seem to understand it." Regulators have done poorly in communicating to SROs the risk management objectives of current regulatory regimes. Only one country responding to our questionnaire indicated that it has conducted a specific risk assessment of this sector. In addition, the sources of information that responding governments use in assessing risk in a more ad hoc manner skew heavily toward governmental sources rather than information from the affected community.²⁷¹ A number of FIUs responding to our questionnaire indicated that other government agencies engage in outreach to the Somali community for the purpose of social welfare and refugee integration,²⁷² but there was little evidence that financial regulators are working with these other government agencies to craft joint analysis and engagement strategies on SRO issues.

266. Program on Humanitarian Policy and Conflict Research, "Countering Terrorism in Humanitarian Crises: The Challenges of Delivering Aid to Somalia," September 2011 (background briefing for the Informal High-Level Expert Workshop for Government Representatives, 29–30 September 2011) (copy on file with author).

267. Harvey Morris, "UN Says Somali Aid Falling Into Wrong Hands," *Financial Times*, 10 March 2010.

268. See Thompson, *Trust Is the Coin of the Realm*, pp. 270–271. For a deeper discussion of the moral and operational implications of such interactions, see *ibid.*, pp. 272–280.

269. See *ibid.*

270. Survey response no. 2.

271. The number of questionnaire responses identifying each source used to assess risk/shape allocation of resources was: Census data – 0/13; Open source – 7/13; Community visits – 3/13; Bank reporting – 9/13; Law enforcement investigations – 6/13; Domestic intelligence – 6/13; Foreign intelligence – 4/13.

272. Survey response nos. 1, 2, 6, and 11–14.

Indeed, only one jurisdiction indicated it had sought to engage Somali business associations or SROs to generate feedback or input into regulatory arrangements. Furthermore, the resources devoted by financial regulators to education and outreach efforts to remitting communities are extremely low. The Danish FSA, for example, has two people working part-time on these issues. The HMRC has 50 staff visiting 2,700 money service businesses to carry out compliance activities as well as broader outreach. The result, as one regulator admitted to us, is that “[e]ducation and outreach efforts are not resourced to risk.”²⁷³

We found evidence of some positive signs. At least three jurisdictions have formed internal ad hoc working groups to address AML/CFT risks in the SRO area.²⁷⁴ Two of these groups focus on intelligence analysis, and one focuses on sector risk assessment, law enforcement, and intelligence analysis. One jurisdiction among those responding to our questionnaire, plus Australia, are moving toward using a “campaign” approach to communicate with remitters regarding heightened risk in specific remittance corridors.²⁷⁵

Given time, regulators could use these interagency platforms to develop whole-of-government strategies, like that being crafted in the United Kingdom, to develop a more integrated analysis of where risk is located at any given time, to communicate that more effectively to affected money transfer businesses, and to more efficiently allocate resources to risk management.

Because SROs are transnational, regulatory integration may need to occur not only at the national, but also at the international level. Our research suggests that when possible, SROs move operations to jurisdictions where administrative and compliance burdens are lowest. The disaggregation of SROs into multientity groups, encouraged by differences in regulatory arrangements, also reduces transparency. Our interviews and questionnaire revealed that intergovernmental cooperation to understand and improve the regulation of SROs remains in its infancy, heavily dominated by law

enforcement and security agencies. Networking among financial regulators on these issues seems limited by comparison. As one example, many jurisdictions have a criminal record check as part of their licensing procedure. Few of them apparently conduct inquiries routinely to check criminal records of other countries,²⁷⁶ which is surprising, given the highly mobile nature of the Somali business population and the fact that many SRO operators hold dual citizenship or passports.

The net result of this regulatory fragmentation and confusion is that neither licensing nor registration appear to be particularly effective in producing much more than ritual compliance from SROs. If we measure regulatory success by money spent on the cottage industry of AML/CFT consultants, then the regulatory efforts of the last decade have been an undoubted success. If we measure success by a vocal recognition by SROs that compliance with AML/CFT obligations is in their interest, then our research suggests that success is much more tenuous and elusive. Part 3 of this report addresses how we might change that assessment.

273. Personal interview no. 24.

274. *Ibid.*; survey response nos. 1, 8, and 12.

275. Personal interview no. 23; McCusker, “Underground Banking,” p. 5.

276. Personal interview no. 14.

3. Harnessing the Potential of Somali Remittances

THE KEY REGULATORY PROBLEM, SIMPLY FRAMED, is a lack of trust. SROs do not trust that it is in their interest to bear the regulatory burdens regulators require of them in order to manage AML/CFT risks, and regulators and their proxies—the banks—do not trust that SROs are faithfully discharging those burdens. The challenge is to rebuild that trust after a decade of distrust.

Building trust will require coordinated, multijurisdictional efforts by regulators to convince SROs that effective regulation is in SROs' own interest. Regulators must reframe the regulatory discussion and find short-term projects on which they can partner with SROs to build mutual confidence, which in time may blossom into trust.

The key to more effective regulation that better harnesses the potential of Somali remittances is capitalizing on trust and recognizing that, over the mid- to long term, SROs represent reservoirs of social capital—intra- and interclan trust—that might be used to generate a more durable political and economic settlement in Somalia. Regulation should be reframed not only in terms of AML/CFT risk management, but also in terms of confidence building and ultimately Somali state building. SROs wield enormous political and economic power in the Somali nation. Regulation

should aim to harness that power to foster peace, prosperity, and the enjoyment of human rights in Somalia.

Capitalizing on Trust: From Confidence Building to State Building

Our research suggests that the international community has not yet fully exploited the information at its disposal about the political and economic power of SROs. Working with SROs offers the international community an extraordinary opportunity to use the social capital embedded within Somali trust networks to strengthen confidence between regulators and, in time, perhaps to begin to build intergroup cooperation as the basis of a durable political economic settlement.²⁷⁷

One perspective holds that “the common mistake among those building new institutions [in postconflict settings] is to focus on creating [anonymous trust] while at the same time disrupting the face-to-face networks that are the necessary building blocks for reconstituting trust more widely.”²⁷⁸ An

277. See William Maley, “Institutional Design and the Rebuilding of Trust,” in *From Civil Strife to Civil Society: Civil and Military Responsibilities in Disrupted States*, ed. William Maley, Charles Sampford, and Ramesh Thakur (Tokyo: UN University Press, 2003), pp. 163–179. For a similar argument regarding the potential of hawaladars in Afghanistan, see Thompson, *Trust Is the Coin of the Realm*.

278. Thompson, *Trust Is the Coin of the Realm*, p. 178.

overly antagonistic approach to regulating SROs risks overlooking this opportunity in just this way. “[T]he risk of criminalising major parts of the ‘informal’ sector is that peacebuilders ignore some of the most important potential stakeholders in the restoration of peaceful economic rule.”²⁷⁹ Such networks may represent not only potential enemies, but also, handled properly, potential allies.²⁸⁰

SROs have demonstrated that they hold immense power to finance war and peace in Somalia. For good or bad, remittances “have the potential to alter the local balance of economic, political and military power.”²⁸¹ SROs sometimes play this role independent of remitters themselves, acting not just as a vehicle for others’ actions, but as an actor in their own right. In one case of fighting between two Isaaq subclans in the Ogaden region of Ethiopia, subclan members on each side collected money to fund clan-elder delegations for peace negotiations. Dahabshiil lent some of the money for the conference and was paid back over time by diaspora donations.²⁸²

How could this power be harnessed through regulation for Somalia’s peace, human rights, and prosperity? The key lies in incentivizing SROs to channel funds toward peaceful activities and away from conflict-driving and conflict-sustaining activities such as terrorism. AML/CFT due diligence potentially has a crucial role to play, especially if the existing AML/CFT infrastructure evolves in coming years into a basis for financial institutions, including banks and SROs, to discharge their responsibility to respect human rights, as set out in the UN Guiding Principles on Business and Human Rights.

Two types of incentives—moral and economic—seem likely to be needed to encourage SROs to take ownership of enhanced due diligence efforts. Somali remitters themselves might be susceptible to moral arguments. A recent article describes how, as support for al-Shabaab has dropped away

among older members of the Somali diaspora,²⁸³ Somali remitters appear to be conducting their own enhanced due diligence when they receive requests for remittances to ensure that funds are not passed on to al-Shabaab.²⁸⁴ Perhaps carefully tailored outreach and engagement to certain sections of the Somali diaspora could help encourage Somali remitters to favor those SROs that will work to protect human rights and foster peace and prosperity in Somalia, i.e., those that will take ownership of enhanced due diligence efforts.

Economic incentives could also be created with a bit of imagination. In Afghanistan, the government has restricted foreign exchange auctions to those money service businesses that have registered with the government, creating strong incentives for registration.²⁸⁵ A similar arrangement might be feasible in Somalia if donors and international partners such as the United Nations could agree with the various potential regulatory bodies, such as the Somali Central Bank and bodies in Somaliland, Puntland, and potentially other local authorities, on how regulatory responsibilities and any resulting revenues would be allocated. Other economic incentives might be found by identifying areas where inter-SRO cooperation will be a necessary prerequisite for each SRO to have access to an increased payoff. There are three areas where this may be the case: the creation of a diaspora bond, with the backing of SROs; the development of a mobile financial services plan for Somalia in which interoperability between different SRO and telecom networks will maximize payoffs for all; and the development of a Somali financial reconstruction roadmap, with SRO participation.

Because they are built out of the trust networks embedded within Somali jilib and clan groups, SROs represent a fertile ground for developing such cooperation and then growing it into a more durable political and economic settlement to underpin Somalia’s future peace and prosperity. Any effort

279. *Ibid.*, p. 250.

280. James Cockayne and Adam Lupel, eds., *Peace Operations and Organized Crime: Enemies or Allies?* (New York: Routledge, 2011).

281. Horst, “Transnational Political Engagements of Refugees,” p. 320.

282. Horst and Gaas, *Remittances for Peace?* pp. 19–20.

283. 2010 Somalia monitoring group report, para. 25.

284. Hammond et al., *Cash and Compassion*, pp. 81–82.

285. Thompson, *Trust Is the Coin of the Realm*, pp. 265–266.

to build financial services in Somalia will require an agreement among SROs about fundamental aspects of governance, such as the authority to levy taxes and governmental revenue-sharing arrangements. Because remittance organizations closely track clans, an interclan agreement around remittance regulation seems likely to offer a modernized version of the *xeer*, the social contract between jilib groups that traditionally provided the glue between Somali clans and lineage segments.²⁸⁶ A partnership among regulators, SROs, and relevant international partners such as the United Nations and World Bank along these lines may offer an alternative route to state building in Somalia.

How Do We Get There? Recommendations for Action

The central argument of this report can be captured in the idea that improving the regulation of Somali remittances requires capitalizing on trust: turning the social capital within SROs into a basis for improved AML/CFT regulation around the world and improved protection of human rights and prosperity in Somalia. In this final section are three areas of action that could make a demonstrable difference in the months and years ahead.

1. BUILDING CONFIDENCE THROUGH A REMITTANCE ROUNDTABLE PROCESS

RECOMMENDATION 1: Regulators and SROs should work together with a relevant international partner, such as UNDP or the World Bank, to establish a Remittance Roundtable Process.

We recommend the creation of a Remittance Roundtable Process that would bring together regulators; financial institutions, especially banks; community groups; law enforcement; and SROs to discuss how the potential of Somali remittances might be better harnessed. These roundtables should occur in East Africa, the Persian Gulf, the United States and Canada, the United Kingdom, and Europe and, if possible, within Somalia itself.

Each roundtable would bring together local stakeholders to develop practical ideas for ensuring that SROs contribute to peace, human rights, and prosperity in Somalia. The aim of these forums would be to move the discussion past the last decade of distrust and reframe regulatory questions as a partnership intended to minimize the AML/CFT and human rights risks involved in the SRO business and to lay the foundation for future Somali peace and prosperity. This would also build on recent recommendations in a study commissioned by UNDP suggesting that UNDP or another international actor assume a role in advocating with and on behalf of SROs²⁸⁷ and on calls from within the U.S. government for more engagement with the Somali diaspora.²⁸⁸

2. REGULATOR-REMITTER COLLABORATION ON JOINT OUTREACH, RISK ANALYSIS, AND EARLY WARNING

RECOMMENDATION 2: A core group of regulators and SROs should work together to develop joint outreach tools explaining Somali remittances to banks and other regulators and joint risk analysis and early-warning tools helping regulators and SROs to discharge their AML/CFT and human rights due diligence obligations.

We recommend that a core group of regulators and SROs work together on a distinct, manageable set of joint, short-term concrete projects to foster improved trust between regulators and SROs. Through our research and

286. Lewis, *Pastoral Democracy*, pp. 4–6; Mohamed, “Kinship and Contract in Somali Politics,” pp. 226–249.

287. Hammond et al., *Cash and Compassion*, pp. 86–87.

288. See Josh Richardson, “The Somali Diaspora: A Key Counterterrorism Ally,” *CTC Sentinel* 4, no. 7 (July 2011): 12–14, <http://www.ctc.usma.edu/wp-content/uploads/2011/07/CTCSentinel-Vol4Iss74.pdf>.

consultations, we have identified two particular areas where progress might rapidly be made.

First, in the area of **joint outreach tools**, numerous regulators and nearly all banks currently lack access to accurate, up-to-date information explaining how the Somali remittance industry works. A small group of regulators and SROs could work together to produce a set of materials explaining how the industry typically operates to dispel some of the myths that surround it. A cooperative effort to produce and disseminate these materials could significantly build confidence between those engaged in the effort and among the broader financial and regulatory community about Somali remittances.

Second, in the area of **joint risk analysis and early warning**, regulators and SROs could share information on a recurring basis about which communities in Somalia are most affected by armed conflict and terrorism. This collaboration would allow regulators and SROs to develop a more detailed understanding of where in the global Somali remittance network AML/CFT and human rights risks are present at any given time, allowing them to more efficiently allocate their resources for KYC and enhanced due diligence efforts, especially around PEPs. Collaboration could produce a number of open-source risk analyses and early-warning tools that could be of use to a wide number of actors, such as

- a regularly updated **matrix** mapping SRO sending and paying-out activities against different jurisdictions, possibly including contact details for relevant contacts in each jurisdiction;
- a regularly updated **list of Somali PEPs** to help guide SROs, banks, and regulators on how to handle those individuals;²⁸⁹ and
- a set of shared **due diligence training tools**, possibly including an **annual training webinar for officials**

from national and international regulators, banks, and SROs themselves, on the discharge of AML/CFT and human rights due diligence obligations.

Partnership on the development and delivery of these tools is likely to substantially build confidence between regulators and remitters and help strengthen cross-border communication between regulators. In time, this is likely to have substantial payoffs in terms of information sharing, engagement, and regulatory performance.

Where possible, this collaboration should cover not only existing AML/CFT frameworks, but also the new **UN Guiding Principles on Business and Human Rights**,²⁹⁰ which all financial institutions will be incorporating into their due diligence systems in the future. These Guiding Principles, unanimously endorsed by the UN Human Rights Council,²⁹¹ set out states' duty to protect human rights from harm by business and businesses' own responsibility to respect human rights. Preparatory work leading up to the adoption of those Guiding Principles made clear and states have accepted that this means that the financial sector, including banks and small financial operators, must undertake human rights due diligence to discharge their responsibility.²⁹² A lack of control over how fungible assets are ultimately used is not a valid reason for financial organizations to ignore such use.²⁹³ Regulators, banks, and money transfer businesses generally, including SROs, which are likely to be among those clients of banks most impacted by the application of the Guiding Principles because of the high risk of financing human rights abuse in sending funds to Somalia, will need to work together to consider how to apply the Guiding Principles to this sector. A number of major financial institutions working together in the Thun Group, including Barclay's Bank, which is the primary provider of financial services to SROs in East Africa,

289. One possibility would even be for any given jurisdiction to consider treating this list as authoritative, in the sense that a financial institution that followed the guidance provided by this recurring Somali PEP list in determining whether a customer required enhanced due diligence would have a complete defense against allegations of breaching its KYC obligations. The United Kingdom allows SROs to rely on Guidance Notes published by government regulators, after input from the Joint Money-Laundering Steering Group (www.jmlsg.org.uk) in just this way. Personal interview no. 24.

290. UN Human Rights Council, *Guiding Principles on Business and Human Rights*.

291. UN General Assembly, *Human Rights and Transnational Corporations and Other Business Enterprises*, A/HRC/RES/17/4, 6 July 2011.

292. See UN General Assembly, *Promotion of All Human Rights, Civil, Political, Economic, Social, and Cultural Rights, Including the Right to Development*, A/HRC/11/13, 22 April 2009, paras. 72–73.

293. *Ibid.*, para. 51.

are currently studying application of the Guiding Principles to their operations.²⁹⁴ A focus on SROs might be built into that process with some encouragement from those countries that are most focused on both the Guiding Principles and SRO regulation, such as Denmark, Norway, Sweden, the United Kingdom, and the United States.

3. HARNESSING THE POWER OF REMITTANCES FOR SOMALI RECONSTRUCTION

RECOMMENDATION 3: The UN Political Office for Somalia (UNPOS), UNDP, or the World Bank should work with SROs and relevant political authorities in Somalia to develop Diaspora Bond offerings to fund local development projects, a Mobile Financial Services Plan, and a Financial Reconstruction Roadmap.

Finally, we recommend that UNPOS, UNDP, or the World Bank take the lead in working with SROs to undertake a set of **longer-term Somali state-building activities** in which Somali remittances might play a central role.

It has long been recognized that one path out of conflict in Somalia might be to create sufficiently strong economic incentives for cross-clan cooperation—a peace dividend. Numerous observers have noted that remittance organizations must play a key role in any such effort. “A professionalized and formalized remittance sector is the key to sustainable stability and governance, effective reconstruction and improved livelihoods in Somalia.”²⁹⁵ As the hot war-fighting winds down, remittances are likely to be the major source of funds for reconstruction and development, apart from official development assistance and a few big-ticket investments, mainly around port infrastructure and the extractives sector. A careful partnership among international donors and regulators, local governmental authorities, and Somali businesses, including

SROs, seems likely to be crucial to sustaining peace. SRO cooperation on financial reconstruction may also offer a path to interclan cooperation, out of which a more stable political-economic settlement might be generated. SROs retain a close relationship with clan structures and the system of financial solidarity within jilib groups. Traditionally formal agreements between those groups structured the Somali social contract (xeer). Therefore, an agreement among SROs about how to work together on Somali financial reconstruction and related issues, based on xeer, might provide the basis for broader interclan cooperation around regulatory and revenue-sharing issues. In time, this could offer a more effective path to state building in Somalia.

UNPOS and the World Bank could work with SROs on three projects to harness the potential of Somali remittances. First, working with appropriate political authorities in Somalia, whether the TFG or the Somaliland, Puntland, or Gulmudug administrations, UNPOS and the World Bank could work toward **Somali Diaspora Bond offerings**. Ethiopia has issued several diaspora bonds to fund infrastructure projects, and the World Bank is currently advising Kenya on a similar offering. A diaspora bond may be a more productive use of diaspora funds than direct remittances because it would allow governmental authorities to address public infrastructure and service needs that remittances do not appear to address and would help to reinforce the centralized budget process underpinning governmental processes. Diaspora bonds may be a better source of capital for governmental authorities than the open market because the diaspora is likely to accept a lower yield and later maturation date than the market might. Diasporas are patriotic, patient, and less sensitive to currency and political risk.²⁹⁶ Such a project would need to be developed in close partnership with an appropriate external financial advisor, such as the World Bank. SROs would play a key role in marketing the bond and might be incentivized to do so through some cofinancing role.

294. Thun Group, “Statement by the Thun Group of Banks on the ‘Guiding Principles for the Implementation of the United Nations ‘Protect, Respect, and Remedy’ Framework’ on Human Rights,” 2011, <http://www.business-humanrights.org/Links/Repository/1009095/jump>.

295. Waldo, “Somalia Remittances,” p. 22.

296. “Diaspora Bonds: Milking Migrants: How Poor Countries Can Tap Emigrants’ Savings,” *Economist*, 20 August 2011, <http://www.economist.com/node/21526324>.

Perhaps the greatest challenge would be identifying which Somali governmental authorities would participate in the project. Careful attention to the relationship between different authorities, clans, and SROs would be needed and would be well served by the matrix proposed in Recommendation Two. Yet, it may prove controversial for UNPOS and the World Bank to work with authorities other than the TFG for such an international offering. At the same time, the TFG has only very limited capacity to deliver developmental projects that such an offering might underwrite. Accordingly, one alternative would be excluding any public authority from the bond offering, apart from agreeing to the necessary approvals of the development project, and simply having the bond issued by a consortium of SROs as a private offering, perhaps underwritten by the International Finance Corporation.

A second project would involve the development of a **Mobile Financial Services Plan** for Somalia. An international sponsor such as UNPOS, UNDP, or the World Bank would bring together SROs, Somali telecoms, and financiers to develop a plan for the countrywide rollout and development of mobile financial products and services, building on the ZAAD and SAHAL and other service offerings already in place. As with the development of a Diaspora Bond offering, this project would offer SROs strong incentives to cooperate across clan lines because internetwork interoperability will offer all mobile money providers greater payoffs in the long term.

Third, the same international actors could engage SROs and other relevant actors in developing a **Financial Reconstruction Roadmap** for Somalia. The aim would be creating a long-term roadmap to build Somali access to financial services, meet the Somali business communities' financing needs, and lay the foundations of a sustainable economic settlement in Somalia. SROs have strong incentives to work together to develop such a roadmap because they stand to benefit significantly from any Somali postconflict growth. SROs will likely transform into Somalia's banks, offering a wider spectrum of services to small, midsize, and even large entrepreneurs. Indeed, Dahabshiil has already opened a bank in Djibouti.

Once again, perhaps the key issue to be addressed is the relationship between governmental power, particularly the authority to levy taxes, and the allocation of revenues within Somalia. The development of a Financial Reconstruction Roadmap might well be something that should be built off the back of a narrower sectoral revenue development and sharing plan, for example, in the remittance sector. Such an agreement could be developed working with SROs narrowly; a range of governmental authorities may need to be engaged later to develop that sector-based revenue-sharing agreement into the broader arrangement needed to underpin broader financial reconstruction.

Cooperation among SROs on all of the preceding projects—joint risk analysis and due diligence tools, PEP lists, a diaspora bond offering, and a mobile financial services plan—would lay the groundwork for this final project. Cooperation among SROs, particularly with Somali and foreign regulators, would create the basis of trust on which this would capitalize. In turn, these projects may offer opportunities for harnessing the power of Somali remittances for counterterrorism, human rights, and prosperity in that country and abroad.

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Appendix 1: Personal Interviews and Survey Responses

PERSONAL INTERVIEWS

1. Managing director of UK arm of multinational commercial Somali remittance organization (SRO), London, June 2011
2. Manager of UK operations of retail SRO, London, June 2011
3. CEO/director and operations manager at a non-Somali money transfer business, London, June 2011
4. Operations manager and co-owner of commercial foreign exchange company, Dubai, July 2011
5. Director and sole owner of retail SRO, Dubai, July 2011
6. Assistant general manager at a Somali import/export trading company, Dubai, July 2011
7. Managing director and database administrator at a multinational retail and commercial SRO, Dubai, July 2011
8. Regional business development director at the headquarters of a multinational commercial and retail SRO, Dubai, July 2011
9. Supervisor at a multinational commercial and retail SRO, Dubai, July 2011
10. CEO and Somalia business director of Somali conglomerate and commercial SRO, Dubai, July 2011
11. Managing director of family network SRO catering primarily to non-Somali clients, Dubai, July 2011
12. Remittance department manager at a non-Somali foreign exchange house, Dubai, July 2011
13. Representative of a national money transfer business professional association, July 2011
14. Senior regulatory officials from OECD country, March 2011
15. Senior East African regulatory officials, June 2011
16. AML/CFT consultant to SROs, Nairobi, May 2011
17. Officer responsible for anti-money laundering training at a retail and commercial SRO, London, June 2011
18. Office manager of high street foreign exchange bureau that deals with retail SROs, Nairobi, May 2011
19. Operations manager of a commercial SRO, Nairobi, May 2011
20. Agent for a family network SRO and foreign exchange house, Nairobi, May 2011
21. Two managers from a multinational retail and commercial SRO, Nairobi, May 2011
22. Regional head agent for a retail SRO, Nairobi, May 2011
23. Regulatory officials from OECD country, June 2011
24. Senior officials at regulatory agencies in OECD country, June 2011
25. Manager at a high street foreign exchange bureau, Nairobi, May 2011
26. Senior regulatory official from OECD country, July 2011
27. Intelligence officer from OECD country, March 2011

SURVEY RESPONSES

Survey responses were received from financial intelligence units in Belgium, Canada, Denmark, Finland, India, Israel, Italy, Lebanon, Netherlands, Norway, Spain, Sweden, United Kingdom, and Yemen. In order to maintain confidentiality, we refer to these responses as survey response 1 through survey response 14. This numbering system does not correspond to the order of responses listed above.

Appendix 2:

Online Financial Intelligence Unit Questionnaire

Part A. How do people send money to, or receive money directly or indirectly from, Somalia in your jurisdiction?

1. Development

- How did the practice of sending money to or from Somalia commence in your jurisdiction?
- How has this practice changed over time?
- Are you aware of any particular social, business or other obstacles specific to Somali money transfers in your jurisdiction?

2. Presence and activity

- What is the size of money transfer flows from your jurisdiction to Somalia each year? (Numbers of people remitting, numbers of remittance transactions, value remitted.)
 - Does your jurisdiction receive transfers which create secondary transfer flows to Somalia (i.e., from Somali diaspora communities in another jurisdiction, routed to Somalia through your jurisdiction)? If so, what is the average number and size of these transactions per year?
- How is the market for sending money from your jurisdiction to Somalia serviced—by family-based remittances, collectives, charitable associations, or commercial operations?
 - How many of each kind of organization servicing the Somali remittance market are there in your jurisdiction?
 - How much is moved through each channel each year (smallest, largest, average)?
 - What are their revenues (smallest, largest, average)?

3. Market segmentation

- Do different organizations specialize in movements of money to particular areas and/or from particular areas in your jurisdiction, or work with particular client-bases?
- Are different Somali remittance organizations connected with partners in other jurisdictions? If so, how—by franchise, parent/subsidiary relationship, personnel movements, trade association ties?
- How do organizations transfer value? Are there identifiable corridors that they move value through?

Part B. Somali money transfer organization interactions

4. Relationship to remitter and beneficiary communities

- How do Somali remittance organizations interact with local communities?
 - If *payment/sending community*, what are the entry points—kiosks, agencies, mobile agents, online, collecting accounts, community organizers, mosques?
 - If *beneficiary/receiving community*, how are payments distributed—through agents? Banks? Other?
 - Is there a history of philanthropy among these organizations within the local community, or are they otherwise seen as part of a welfare system—e.g., through involvement in humanitarian assistance, micro-credit, development or other activities?

5. Relationship to each other

- How do these organizations interact within your jurisdiction? Do they compete, or do they have distinct niches?
- Are there collective or cooperative activities—such as cooperation in dealing with or advocating to regulators? Is there a trade or professional association of some kind?

6. Bank relations

- What kind of relationship, if any, do organizations sending money to Somalia from your jurisdiction have with local and foreign banks?
- Do local banks provide these organizations a full range of banking services? If not, why not?
- Are these organizations seen as posing AML risk for local banks? If so, why?

7. Government relations with Somali money transfers

- Beyond AML/CFT compliance (addressed below), does your government have other forms of contact, including dedicated programs, with organizations facilitating the transfer of money to Somalia? If so, for what purpose? (Please describe the nature of these forms of contact, and the resources involved, for each of these areas where applicable):
 - Prudential, market stability or consumer protection
 - Policing
 - Intelligence and security
 - Immigration and integration
 - Education and training
 - Other

8. Government relations with trade/business associations

- Has your government sought to engage Somali business associations (especially involving money transfer organizations)? If so, on what issues, e.g.:
 - to generate feedback on or input into regulatory arrangements
 - on remitters' compliance with AML rules
 - to conduct training on AML/CFT
 - in the course of regulatory impact assessments
 - regarding humanitarian assistance or development concerns
 - Other

Part C. Regulating Somali money transfers

9. Regulatory objectives

- What are the objectives of your jurisdiction's existing regulatory regime? (Please indicate for each one where these objectives are stated or identified.)
 - AML/CFT
 - Prudential/market stability
 - Providing accessible financial services
 - Consumer protection
 - Development (overseas aid and assistance)
 - Broader national security objectives
 - Other
- What provision, if any, do existing arrangements make for balancing these objectives in government agencies' interactions with Somali money transfer organizations?

10. Regulation

- Please describe how money transfers to Somalia from your jurisdiction are regulated.
- What role if any do international standards such as those produced by FATF play in this regulation?
- Is there a harmonization of regulatory procedures between local/state/federal laws and between agencies? If so, how?
- Please describe the resources (budget, personnel) available to regulatory agencies in your jurisdiction to regulate the transfer of money to Somalia, with reference to AML/CFT standards.
- Please describe the sources of data you use to shape agencies' programming and resource allocation regarding Somali remittance regulation, e.g.:
 - census data
 - open source (media, academic sources, international organizations, conferences)
 - on-site community visits
 - bank reporting
 - law enforcement investigations
 - domestic intelligence
 - foreign intelligence

11. Regulatory requirements—registration, licensing & software

- Are there specific requirements for an organization that transfers money to Somalia to be registered and/or licensed?
- Are these organizations required to provide bond deposits or securities in order to conduct business or be eligible for registration/license? If so, in what amount? To whom?
- What information must an applicant provide to receive and/or renew a registration and/or license?
- How is application information gathered? How long does gathering that information usually take? How is this information tested?
 - Information about directors? Managers? Staff?
 - Is there a character test—and if so, what is it? How does that differ (if at all) from other types of financial business in your jurisdiction?
 - What due diligence is provided on the information provided? Is it run against UN sanctions lists? Against national criminal databases? Against foreign or Interpol criminal databases?
- Is this information shared with other agencies? If so, under what terms?
- Are there specific regulatory requirements relating to technology, software, or data management?

12. Regulatory requirements—KYC, SARs and politically exposed people

- What are these organizations expected to do in terms of applying Know Your Customer rules?
- How does the government receive, handle and analyze suspicious transaction reports relating to money transfers to or from Somalia, or other jurisdictions remitting into Somalia? Which agencies lead the analysis? Are results of the analysis shared with the reporting organization?
- Does the government communicate concerns about heightened risk associated with particular individuals or corridors to organizations transferring money to Somalia? If so, how?
- How should Somali money transfers identify Politically Exposed Persons (PEPs)? What should they do with that information?

13. Information sharing and analysis

- How is information about Somali money transfers shared and analyzed within government? Are there mechanisms for inter-agency information sharing, joint analysis or consultation?
 - Do these relate to risk assessment, joint law enforcement investigations, or intelligence analysis?
 - Has your jurisdiction conducted a risk assessment of the industry or specific sectors of it?
 - If yes, how was this organized? Who was involved? Is there any provision for this process to be repeated?
 - If no, are there any clear obstacles to such a risk assessment being performed?
- Have conclusions from any previous risk assessment led you to make changes in regulatory procedures or processes? If so, how?

Part D. The future

14. Future market dynamics

- How do you anticipate money transfers to and from Somalia may change in the years ahead?
 - What will the impact of money transfer businesses such as Western Union be?
 - What will the impact of electronic/mobile money be?
 - What will the impact of passporting be?
- Are the AML risks associated with remittance businesses likely to become more or less pronounced, or stay the same? Why?

15. The future of regulation

- Are there weaknesses in your jurisdiction's understanding of or interaction with Somali money transfer organizations that you would like to see addressed? If so, what are they? How could they best be addressed?
- Are there opportunities for strengthening the sector—e.g., through collaborative regulation and/or capacity-building by multiple government agencies, or even multiple governments? In which areas (e.g., software, harmonized regulatory requirements, industry coordination)?

Somalia is struggling with drought, war, piracy and terrorism. Yet the Somali diaspora community offers a lifeline, remitting home some \$1–1.5 billion each year. How to ensure these remittances support an end to war and drought and help to rebuild the Somali state, rather than supporting piracy, terrorism and the fracturing of Somalia? This report offers new analysis of the Somali remittance industry and ideas for improving its regulation, including combating money laundering and countering terrorist financing and supporting state-building. Trust is central to this industry's business model, and trust, the report argues, is the key to improving its regulation.

“The people of Somalia have suffered from the ravages of war for over two decades. It is a community whose survival instincts are exemplary to us all. This report ‘Capitalizing on Trust’ addresses the core activities that have enabled innocent Somali people to survive the suffering brought about by war. It will go a long way in enabling policy makers in the Eastern Africa region and the global community to engage constructively with Somali diaspora communities to help rebuild Somalia.”

— DR. ELIAWONY J KISANGA, EXECUTIVE SECRETARY,
EASTERN AND SOUTHERN AFRICA ANTI MONEY LAUNDERING GROUP (ESAAMLG)



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