



KEEPING THE LIFELINE OPEN

REMITTANCES AND MARKETS IN SOMALIA

BY MANUEL OROZCO AND JULIA YANSURA



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ABBREVIATIONS

ACH	Automated clearinghouse
AML	Anti-money laundering
CIA	Central Intelligence Agency
CFT	Combating the financing terrorism
FAO	Food and Agriculture Organization
FSNAU	Food Security and Nutrition Analysis Unit for Somalia
FATF	Financial Action Task Force
FBI	Federal Bureau of Investigation
FDIC	Federal Deposit Insurance Corporation
FinCEN	Financial Crimes Enforcement Network
GDP	Gross domestic product
GMOD	Global Migrant Origin Database
IFAD	UN International Fund for Agricultural Development
MSB	Money service business
MTO	Money transfer operator
NGO	Nongovernmental Organization
OCC	Office of the Comptroller of the Currency
OFAC	Office of Foreign Assets Control
SAR	Suspicious activity report
SDN	Specially designated nationals
UNHCR	The UN Refugee Agency

EXECUTIVE SUMMARY

Each year, Somali migrants around the world send approximately \$1.3 billion to Somalia in an incredible expression of solidarity, faith, Patriotism, and generosity. Of that, approximately \$215 million comes from Somali-Americans and Somalis in the United States—comparable to the total amount of development and humanitarian assistance that the US government sent to Somalia in fiscal year 2012 (\$242 million). These flows, facilitated by Somali-American money transfer operators (MTOs), represent a significant share of Somalia's economy and help reduce Somalia's reliance on assistance from foreign governments and international organizations. Moreover, remittances allow individuals and families to spend money based on their needs and priorities. Continued support from the Somali diaspora is essential for Somalia to successfully emerge from its protracted humanitarian emergency and political crisis, as well as to build the foundations for its long-term development.

During the 2011 drought and food crisis in Somalia, the generosity of the Somali diaspora played a vital role in helping Somali families survive. Unfortunately, when a bank in the United States closed the accounts of several Somali-American MTOs during the crisis, it became clear that money transfers could come to a halt at a moment's notice. Somali-American MTOs constitute a critical link in the remittance chain, transferring funds from the diaspora and distributing cash to recipients throughout Somalia, where Western MTOs and banks have little or no presence.

Somali-American MTOs need bank accounts in the United States to facilitate transfers, but have found it difficult to obtain them in recent years. They have invested significantly in compliance systems, policies, and training to ensure that they do not run afoul of US anti-money laundering/combating the financing of terrorism (AML/CFT) requirements, but most US banks have ignored these investments. In recent years, many US banks have branded Somalia a risky destination for money transfers and have unceremoniously closed the accounts of Somali-American MTOs without providing any specific reasons or justifications. Such closures have occurred at nearly twice the rate that US banks closed Latin American MTO accounts. Account closures have already endangered the lives and livelihoods of Somalis and undermined Somali diaspora communities' confidence in the US government and financial sector. Further closures could have disastrous consequences, up to and including a complete shutdown in the formal remittance system.

Somalia's recovery and stability are extraordinarily fragile. Many Somali families continue to rely on remittances to meet their most basic needs. With roughly a quarter-billion dollars of direct, community-level support at stake, all parties involved—Somali authorities, the US government, banks, and MTOs—must ensure that members of the Somali diaspora in the United States can send their money to Somalia as long as they are willing and able to do so.

Rangeland rehabilitated under Adeso's programs in Midigale, Somalia.

Daniel Gerstle / ©Adeso

RECOMMENDATIONS

BANKS SHOULD EXPAND SERVICES TO SOMALI-AMERICAN MTOS

Sending money to Somalia presents risks to banks, but these risks are neither unique nor insurmountable. Greater efforts by banks to evaluate Somali-American MTOS' applications on a case-by-case basis will lead to crucial expansions in service for Somalis without a meaningful increase in the banks own reputational or legal exposure.

US POLICYMAKERS SHOULD PRIORITIZE REMITTANCE TO SOMALIA

Even a partial MTO shutdown could threaten Somalia's progress toward peace, security, and sustainable development. US Government officials should prioritize the secure transfer of funds to Somalia and develop contingency plans for shutdowns and reductions in service, bearing in mind that increases in aid are not an adequate substitute for the direct financial flows from diaspora communities that build resilience and address people's needs and priorities directly.

THE US TREASURY DEPARTMENT SHOULD HELP INTEGRATE SOMALI-AMERICAN MTOS INTO AN AUTOMATED CLEARINGHOUSE (ACH)

The clearinghouses would aggregate all transactions originating from all MTOS and agents, thereby helping regulators and MTOS identify remitters sending funds through multiple MTOS to avoid scrutiny. It would minimize redundancies, enhance oversight of local agents, and improve compliance with US sanctions regimes.

MTOS SHOULD IMPROVE TRAINING AND MONITORING OF AGENTS

MTOS should continue to provide agents with diverse and appropriate methods of training to detect suspicious activities. MTOS should also regularly test their agents' performance, keep documentation of all trainings and tests at their headquarters and regional offices, and carry out regular site visits.

MTOS AND REGULATORS SHOULD COLLABORATE ON BEST PRACTICES

Although identifying a set of best practices would be useful for all MTOS, it is particularly needed by Somali-American companies. In addition to promoting a set of uniform compliance policies and procedures, it would help rehabilitate the image of MTOS in the US by directly addressing the fears and negative perceptions held by some banks.

MTOS SHOULD DEVELOP MOBILE MONEY TRANSFER TECHNOLOGY FOR SOMALIA

Currently, at least three Somali mobile network providers have developed their own individual money transfer platforms within Somalia. Somalis are already using mobile technology to pay for goods and services.

THE US GOVERNMENT SHOULD HELP SOMALIA REGULATE ITS PAYMENT SYSTEMS

Through technical assistance and capacity-building measures, the US government can greatly help Somalia improve its payment system infrastructure.

SOMALI AUTHORITIES SHOULD ACTIVELY REGULATE INTERNATIONAL MONEY TRANSFERS

Passing regulations to prevent money laundering and the financing of terrorism would demonstrate Somalia's willingness to listen to the concerns of international partners, as well as build the confidence of banks.



INTRODUCTION

This report investigates the obstacles facing the free and secure flow of remittance transfers from the United States to Somalia. Banks in the US perceive Somalia as a risky destination for money transfers, and, as such, have branded Somali-American money transfer operators (MTOs) as high-risk clients. We find that this blanket conclusion is not based on fair and individualized assessments of MTOs' respective anti-money laundering policies and procedures, and has served as the basis for unnecessary MTO account closures. These account closures may result in a substantial disruption to Somalia's recovery and economic growth.

Remittances to Somalia amount to approximately \$1.3 billion a year, 16 percent of which comes from the United States. Remittances are a lifeline for many Somalis, providing them with a means to meet their immediate needs for food, shelter, clothing, and other basic necessities as well as open and sustain small businesses, send children to school, and invest in their communities. Remittances to women, in particular, result in investments in education, health, and nutrition.

In the United States, small and midsize Somali-American MTOs provide most remittance services to Somalia. These businesses offer basic cash-to-cash services at a relatively low cost. They specialize in personal, trust-based relationships with customers. Most of the MTOs have developed ways to deal with the unique challenges of sending money to Somalia, a country with security challenges, weak infrastructure, and minimal regulation.

Somali-American remittance companies face a challenging regulatory environment, particularly with respect to anti-money laundering and combating the financing of terrorism (AML/CFT) requirements. Somali-American MTOs actively seek to comply with US regulations and have made significant strides toward reducing risk through monitoring, record keeping, and agent training.

Still, the Somalia remittance pipeline is under serious threat. Despite their efforts, Somali-American MTOs are often perceived as representing a high risk for illegal activities, such as the financing of groups and individuals listed by the US government as terrorists. Many banks have closed MTO accounts, making it difficult for MTOs to maintain operations, disrupting remittances from the US to Somalia, and, in particular, jeopardizing the survival of Somali families during the 2011 famine. Further bank account closures could result in a total remittance cutoff, which would endanger more Somali lives and interrupt economic development in the country as a whole. If all the stakeholders—the Somali authorities, the US government, US banks, and Somali-American MTOs—make a concerted effort, they can prevent these disruptions and greatly enhance the security of the remittance system. This report offers recommendations to achieve these goals.



A woman obtains cash through a money transfer operator in Badhan, Somalia.
Daniel Gerstle / ©Adeso

METHODOLOGY

This report is based on semistructured interviews conducted on behalf of Oxfam with individuals knowledgeable about the Somali remittance industry. These individuals included money transfer executives, midlevel managers, compliance officers, and agents, as well as customers, community leaders, professionals in the humanitarian field, religious leaders, Islamic law experts, US government regulators, elected representatives, and other businesspeople. Interviews were conducted in Minnesota, Ohio, the United Kingdom, and the United Arab Emirates (UAE) in person and by phone from February through April 2013. Some MTO interviews were conducted at the interviewee's place of work, which allowed additional insights into standard operating procedures, compliance, and community relations. This report also draws on original research commissioned by Adeso, which consists of interviews in south-central Somalia, Puntland, Somaliland, Dubai, and Nairobi with executives and agents in the money transfer industry and consumers. Owing to the sensitive nature of the topic, interview sources remain anonymous.

MIGRATION AND REMITTANCES IN SOMALIA

INTERNATIONAL MIGRATION

Although Somalis have long engaged in labor migration, departures from the country accelerated greatly as a consequence of to the civil war in the late 1980s and early 1990s that left nearly a million refugees in various countries around the world. The ongoing fighting in Somalia between rival factions has ensured high rates of migration over the past two decades.

Currently, there are an estimated there are over 600,000 Somali migrants worldwide, and possibly considerably more.¹ This population has scattered across Europe and the United States as well as several African countries, including neighboring Ethiopia and Kenya, which have sizable ethnic Somali populations of their own. Table 1 shows the estimates of migrants according to country of destination, as identified by the Development Research Centre on Migration, Globalisation, and Poverty's Global Migrant Origin Database (GMOD) and the World Bank.² The figures in the table exclude Somalis in refugee camps. The UN Refugee Agency (UNHCR) reports that there are more than one million refugees in neighboring countries.³

The United States is a major destination for Somali migrants, particularly resettling refugees. The US Census Bureau's 2011 American Community Survey reports that approximately 127,000 people of Somali ancestry are living in the US, 91,000 of whom are foreign-born.⁴

Somalis are concentrated in a few US states and cities. The 2011 Census Bureau report indicates that approximately 38,000 people of Somali ancestry live in Minnesota, with the majority in the Twin Cities metropolitan area, and significant numbers are in smaller Minnesotan cities such as Rochester and St. Cloud.⁵ Somali populations can also be found in Ohio, Washington state, and California.⁶

Remittances enable Somali families to mitigate poverty and, in many cases, help them fulfill their immediate needs for food, shelter, clothing, and other basic necessities.

TABLE 1. SOMALI INTERNATIONAL MIGRANTS

COUNTRY OF DESTINATION	GMOD, 2007	WB, 2010
Ethiopia	223,233	161,179
United Kingdom	50,849	110,326
United States	43,529	109,618
Germany	25,091	11,144
Netherlands	24,978	13,521
Saudi Arabia	24,030	27,252
Canada	23,432	22,718
Sweden	17,030	17,948
Kenya	16,189	55,246
Denmark	13,414	13,230
Norway	12,231	15,465
Other destinations	145,000	255,627
TOTAL	619,008	813,273

Source: Development Research Centre on Migration, Globalisation, and Poverty's Global Migrant Origin Database (GMOD), 2007, and World Bank (WB) data, 2010.

FIGURE 1. METHODS OF ESTIMATING REMITTANCES TO SOMALIA

REMITTANCE ESTIMATE METHOD 1:						
Share of households receiving	X	Number of Somali households	X	Annual amount received	=	Remittances received
60%	X	1,246,000	X	\$1,700	=	\$1,271,076,923
REMITTANCE ESTIMATE METHOD 2:						
Share of migrant senders	X	Number of Somali migrants per country	X	Annual amount sent	=	Remittances sent
80%	X	varies (see Table 2)	X	varies (see Table 2)	=	\$1,297,004,185

REMITTANCES TO SOMALIA

Conflict, resource scarcity,⁷ and economic disruptions have made Somalia particularly reliant on remittances. Money from abroad can have positive impacts on entire communities. It is sometimes distributed to additional community members via loans and charity, according to several sources. In some cases, remittances support efforts at the municipal or regional levels, contributing to infrastructure projects such as the development of water-filtration systems, payment of teacher salaries, and construction of schools and hospitals.

Moreover, remittances enable Somali families to mitigate poverty, and, in many cases, remittances help them fulfill their immediate needs for food, shelter, clothing, and other basic necessities. One customer explained that his monthly remittance of \$400 to his mother- and sister-in-law's household supports food costs for six people who have no other source of income and pays for private-school education for three nieces and nephews, one of whom is about to start university and none of whom would be able to attend any school without financial help. In the absence of remittances, he says, he would be unable to "ensure a middle-class existence for [his] family in Somalia." A recent study commissioned by the Food and Agriculture Organization's (FAO's) Food Security and Nutrition Analysis Unit for Somalia (FSNAU) found that one-third of remittance recipients in Somaliland and Puntland would be unable to afford food, medicine and school fees without their remittances.⁸ The same study found that households receiving remittances are more likely to support poorer families (75 percent) than households not receiving remittances (54 percent).

In 2011, drought, conflict, and rising food prices led the UN to declare a famine in parts of southern and central Somalia. It affected millions and killed approximately 258,000, including

TABLE 2. CHARACTERISTICS OF SOMALI REMITTANCE RECIPIENTS

ORIGIN OF REMITTANCE (COUNTRY)	MIGRANT SENDERS	ANNUAL AMOUNT SENT (PER MIGRANT)	ANNUAL AMOUNT
USA	56,286	3,800	213,888,595
UK	48,616	3,342	162,458,204
Germany	23,989	4,383	105,137,834
Netherlands	23,881	3,513	83,903,243
Sweden	16,282	3,746	60,993,661
Canada	22,403	2,185	48,957,230
Denmark	12,824	3,569	45,768,062
Saudi Arabia	22,975	1,455	33,434,301
Norway	11,694	1,657	19,376,297
Italy	8,220	1,196	9,834,107
Australia	4,082	2,284	9,325,770
New Zealand	1,955	3,538	6,917,293
France	1,551	1,663	2,579,236
UAE	1,714	1,357	2,325,771
Spain	152	1,899	288,741
Other Countries ⁹	351,297	1,400	491,815,842
Total Received	607,922		1,297,004,185

Sources: GMD, 2007, for the number of migrant senders per country, and IFAD, *Sending Money Home to Africa*, 2009, for the amount sent per migrant. Note: The number of migrant senders is based on an estimate that 80 percent of migrants send money.¹⁰

more than 133,000 Somalis under 5 years of age.¹¹ Horrific as it was, the situation would have been much worse had the Somali diaspora been unable to send help. One Somali-American described providing increased financial support not only for his immediately family in Somalia, but also for casual acquaintances who called to ask for food money.

It is difficult to accurately estimate the total amount of remittances to Somalia. Calculations range from \$750 million to \$1.6 billion annually,¹² but it is difficult to find documentation to support such estimates. A World Bank study on Somalia estimated remittances of \$1 billion in 2005. But the study also reported that the average remittance transaction was \$200, implying that at least 500,000 money transfers to Somalia took place. This claim cannot be substantiated.¹³

The flow of remittances can be calculated by examining several different sources: GMOD's estimate of Somali migrants, a 2009 survey of remittance recipients in Somalia carried out for the UN International Fund for Agricultural Development (IFAD),¹⁴ and data on average amounts of money sent as reported in interviews by MTOs.

Using these sources, the total amount of remittances can be calculated in two ways, as shown in Figure 1. The first method is to multiply the number of people who claim that they received remittances by the annual average received.¹⁵ The second method is to multiply the number of migrant remitters by the annual average amount sent. Both methods yield a total of \$1.3 billion per year in remittances.

Nearly 20 percent of remittance flows to Somalia come from the United States, which is the single largest source of these funds, as Table 2 shows. The countries listed in the table are those identified by remittance recipients in Somalia as the main places from which they receive money.

Without reliable data on Somalia's economy, it is difficult to calculate remittances as a percentage of gross domestic product (GDP), though it is undoubtedly substantial. Somaliland officials told Oxfam that remittances constitute 25-40 percent of its GDP, and the figure is likely to be similar in south-central Somalia. Regardless, Somalia receives more in an average year in remittances than it received in humanitarian assistance in

Humanitarian and development assistance from the United States government to Somalia in fiscal year 2012 amounted to \$242 million, just over the \$215 million that we estimate Somali migrants in the US send annually in remittances.

2012 (\$861 million), a year in which donors provided Somalia with an unusually high amount of money to aid recovery from the 2011 drought.¹⁶ Humanitarian and development assistance from the US government to Somalia in Fiscal Year 2012 amounted to \$242 million,¹⁷ just over the \$215 million that we estimate Somali migrants in the US send annually in remittances.

CHARACTERISTICS OF REMITTANCE RECIPIENTS

According to the IFAD survey, 69 percent of respondents said that they had a relative abroad. Of those, 85 percent said that they received remittances, predominantly from Europe and the United States. Sixty-five percent of respondents reported having more than one relative abroad.¹⁸

BOX 1. SNAPSHOT: SOMALI REMITTANCE RECIPIENTS

- 51 percent are women;
- A large majority are employed, particularly in such professions as teaching and entrepreneurship;
- Remittances account for 60 percent of their average annual incomes of \$3,000;
- Most have at least a high school education, and 25 percent of those recipients in their early 40s have some college education; and
- Most have relatives who left Somalia in the mid-1990s and who have been regularly sending money ever since.¹⁹

REMITTANCES, GENDER, AND DEVELOPMENT IN SOMALIA

Worldwide, remittances typically have some impact on local development and the productive base of the local economy. These impacts are mainly the result of asset building, and they are enhanced when women benefit from the flows.²⁰ In general, studies have found that when women receive and control remittances, they are more likely to invest the funds in overall household well-being through increased expenditures on health, education, and nutrition.²¹

In Somalia, remittances are an important source of revenue for women. The IFAD survey found that more than half of Somali women receive money and are responsible for managing house-



A woman buys household goods in Badhan, Somalia. Daniel Gerstle / ©Adeso

hold spending (even when they are not regarded as the head of household). On average, the income of Somali women who receive remittances is 52 percent higher than that of women who do not get funds from relatives living abroad.²²

Although remittances evidently improve the lives of Somali women and their families, it is important not to overstate this impact. As is the case in many other countries, Somali women receive slightly less (5 percent) than men in annual receipts (see Table 3). Also, they depend more on remittances than men: remittances account for 64 percent of their income, compared with 59 percent for men. Finally, female remittance recipients save less money than male remittance recipients.²³

Though Somali women must try to do more with less, there is no doubt that remittances help them achieve greater financial stability, particularly through increased savings. On average, female remittance recipients are nearly four times more likely to save than women who do not receive remittances. Moreover, female remittance recipients are able to save 70 percent more than female nonrecipients. Savings rates are significant because remittances have a substantial positive impact on the ability of households to build assets through savings or investment.²⁴

TABLE 3. CHARACTERISTICS OF SOMALI REMITTANCE RECIPIENTS

	MALE RECIPIENTS	FEMALE RECIPIENTS	FEMALE NON-RECIPIENTS
Annual remittances received	\$1,659	\$1,620	N/A
Annual income (remittances included)	\$3,113	\$2,960	N/A
Remittances as a share of income	59%	64%	N/A
Annual income	\$1,454	\$1,334	\$880
Annual savings rates	39.1%	33.5%	9%
Annual savings contribution	\$574	\$521	\$300

Source: IFAD, *Sending Money Home to Africa*, 2009.²⁵

REMITTING FROM THE US: MARKETPLACE CHALLENGES

REMITTANCES AND THE US MARKET

Approximately 20 money transfer operators (MTOs) send money between the US and Somalia. Most are small to mid-sized Somali-owned businesses that were established in the late 1990s and early 2000s, responding to the civil war in Somalia and the development of Somali refugee communities. Most Somali companies have a fairly limited US presence, with only 15-30 points of service clustered in areas with large Somali populations, such as Minneapolis, Columbus, Ohio, and Seattle. According to their agents, many of these companies also send money to several other East African countries, including Kenya, Ethiopia, Djibouti, and Sudan. However, nearly half of their transfers go to Somalia. Most companies also serve Somali communities in Canada, Western Europe, the Middle East, Australia, and major cities around the world with large Somali populations.

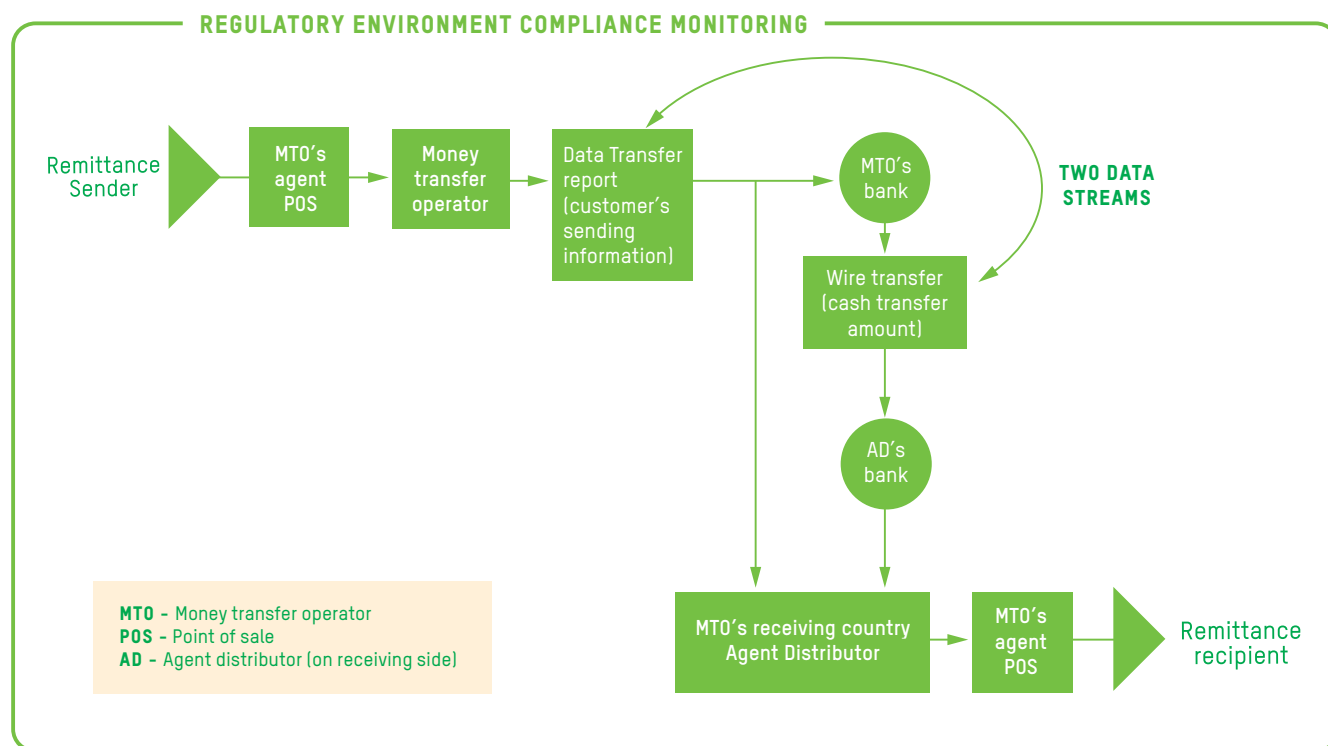
Contrary to the widespread impression that low-income countries such as Somalia have large informal money transfer and payment networks, the majority (73 percent) of remittance recipients obtain their money from established, formal MTOs. According to the IFAD survey, in 2009, 60 percent of recipients received remittances from the three largest companies operating in the region: Dahabshiil, Amal Express, and Qaran Express.²⁶ It is estimated that 27 percent of transfers may be made through informal networks in Somalia, less than in many other African countries, where informality often exceeds 35 percent. This percentage is at least partly because most of the MTOs are Somali companies that gradually expanded their services worldwide and have captured the Somali market for themselves, since the risks associated with operating in Somalia deterred other international money transfer companies from entering the market.

Figure 2 demonstrates how money gets from sender to recipient through an MTO.

REMITTING FUNDS THROUGH A MONEY TRANSFER OPERATOR

1. The sender goes to the office of an agent of the remittance company in the country where she or he resides, providing his or her full details (name and address) and a valid identity document. The sender then provides the cash she or he wants to remit, pays the commission, and provides information about the recipient.
2. The agent screens the names of the sender and the recipient through the Specially Designated Nationals (SDN) List, the US Treasury Department Office of Foreign Assets Control (OFAC) roster of individuals and entities subject to counterterrorism and other sanctions; if the check returns no results, the transaction can proceed.
3. The agent submits the transaction by updating the amount, the sender's details, the recipient's details, and instructions as to where to deliver the funds to a clearinghouse, usually at the MTO headquarters. Submission is generally done electronically.
4. The clearinghouse reviews and confirms that proper due diligence has been followed and, if satisfied, approves the transaction. The details immediately appear on an online database so that the sending agent, the headquarters, and the paying agent can all see the transaction. If the clearinghouse is not satisfied, it suspends the transaction and asks the sending agent to provide additional information.
5. The receiving agent then deposits the cash in a local bank account to be transferred to the company bank account.

FIGURE 2. THE FLOW OF REMITTANCES TO SOMALIA



6. The paying agent views the transaction information and notifies the recipient either by telephone or by text message.
7. The recipient goes to the nearest branch, provides his or her details, proof of identity, and the name and the location of the sender.
8. The paying agent confirms the details given against the transaction records in the database. If the details match and the receiver's identity is confirmed, the agent generates a receipt from the system. Once the recipient signs the receipt, the agent pays the money and the system automatically informs the sender (usually by text message) that the money has been paid to the recipient. The transaction is completed.

CHARACTERISTICS OF SOMALI-AMERICAN MTOS

Most Somali-American MTOs are owned and operated by shareholders, with the exception of Dahabshiil, which is family-owned. Management is usually highly centralized, and tends to be a modified form of franchising. MTOs operate through a network of agents present in major population centers around the world and throughout Somalia. These agents tend to fall into two groups. The first group of agents work exclusively for one MTO as salaried staff and/or receive some

commission based on the volume of transactions they handle. The second group is composed of independent agents who have contractual relationships with one or more MTOs and who are responsible for their own operating costs. According to interviews with MTO agents and executives in Somalia, most agents work exclusively for one MTO.²⁷

Most Somali-American MTOs offer only cash-to-cash services;²⁸ only a handful of businesses have expanded into online services. Generally, Somali-American MTOs focus on building trust and relationships with their consumers for the purposes of their core business, money transfers, rather than attempting to offer a greater quantity of products and services. In interviews, both agents and customers both identified trust as the key to successful money transfer business in Somalia. According to an Imam, mutual trust is an essential component of Islamic law, and, by extension, of Islamic financial services.

MTO executives also noted that Islamic law and reputational concerns require that MTOs avoid transacting with known criminals.²⁹ As one agent in Somalia explained, "Our reputation is at the core of our business success; our ability to attract good employees and customers is dependent on our reputation remaining intact. Even if we do everything else right [but] through a single mistake allow a customer to undertake illegal transactions ... through our branch, we will not only risk our lives but also our reputation could be irreparably damaged."³⁰

The average cost of sending money to Somalia is 5 percent, which falls below the 9 percent average cost of sending remittances globally, and substantially below the 12 percent average cost of remitting to Africa.

The average cost of sending \$200 to Somalia is \$10 (most companies pay out in dollars because the extremely low value of the Somali shilling), meaning the average cost of sending money to Somalia is 5 percent, which falls below the 9 percent average cost of sending remittances globally, and substantially below the 12 percent average cost of remitting to Africa.³¹

Table 4 provides information on some of the biggest Somali-American MTOs.

Somali-American remittance companies often also provide unofficial checking “accounts.” According to interviews with MTO staff, most of the large companies act as unofficial deposit agencies.³² This practice occurs primarily in Somalia, where there is no formal banking sector for individuals or businesses to rely on. However, it also occurs to a certain extent in the Somali diaspora. For example, some Somali migrants in the US debit their Dahabshiil “accounts” when they need to make payments, according to one source. This system has benefits and drawbacks for MTOs. They may be able to use the deposits as working capital, but it may also complicate their bookkeeping. The system offers customers a savings option more secure than “putting the money under the mattress,” but the funds are not insured. Lack of insurance

leaves depositors vulnerable in the event that the MTO goes out of business, as Qaran Express, one of the bigger Somali-American MTOs, did in 2012.³³

DELIVERY CHALLENGES

Companies delivering money in Somalia, a country with poor infrastructure, face unique logistical challenges. For example, travel to rural areas can become impractical during the rainy season, when those roads that do exist can get washed away. Security is also a serious problem in a country experiencing ongoing conflict. One MTO executive explained that customers in Mogadishu have in the past been unable to move freely about the city, so his company had opened receiving points “on every block” to accommodate city residents.

Despite these challenges, MTOs have developed effective means of delivering money. In addition to strong coverage of Mogadishu, Hargeisa, and other population centers, most MTOs have an excellent delivery system for rural recipients, often employing or contracting with agents in low-income and remote areas where the formal financial sector is completely absent.³⁴ “We deliver to literally every corner of Somalia,” one agent claimed.

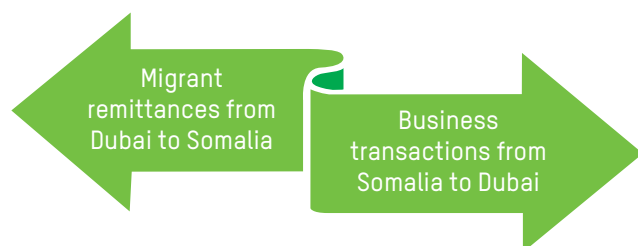
Remittance delivery systems tend to be highly efficient because they are closely linked with business payment systems. In essence, Somali migrants send money home via clearinghouses in Dubai, which then deliver to locations in Somalia through an extensive network of local agents. At the same time, MTOs and their affiliate companies in Dubai play an important role as intermediaries for trading transactions (see Figure 3). The Dubai affiliates send products for sale in Somalia. The aggregate volume of remittances that MTOs pay out in Somalia is often equal to the volume of financial

TABLE 4. BASIC CHARACTERISTICS OF SOMALI-AMERICAN MTOS

MTO	WEB SITE	HQ	YEAR FOUNDED	SERVICE OFFERED	PERCENTAGE FEE (UP TO \$1,000)	COST TO SEND \$200	APPROX. # PHYSICAL BRANCHES
Amaana Express	www.amaanaexpress.com	Dubai	1995	Cash to cash	5%	\$10	15
Amal Express	www.amal-express.com	Dubai	1997	Cash to cash	5%	\$10	30
Dahabshiil	www.dahabshiil.com	Dubai	1970	Cash to cash	5%	\$10	30
Hodan	www.hodan-global.com	Unknown	2001	Cash to cash, online	5%	\$10	15
Iftin	www.iftinuk.com	London	2006	Cash to cash	5%	\$10	5
Juba Express	www.jubaexpress.com	Hargeisa	2009	Cash to cash	5%	\$10	5
Kaah	www.kaahexpress.com	Dubai	2000	Cash to cash	5%	\$10	30
Mustaqbal	www.mustaqbaluk.com	London	1999	Cash to cash	5%	\$10	15
Tawakat Express	www.tawakalexpress.com	London	2003	Cash or check	5%	\$10	35

transactions they send back to Dubai for businesses, making payments convenient for both parties. These are typical financial exchanges that many MTOs carry out with trading companies: they offer their cash payments for trading purposes. These cash flows to and from Dubai are usually very large. One MTO executive estimates that flows to or from larger towns could exceed \$100,000 at a time.

FIGURE 3. THE TWO-WAY FLOW OF REMITTANCES AND BUSINESS TRANSACTIONS



Another challenge associated with transfers is ensuring that the right person is receiving the money. Typically, the delivering agent will ask the recipient to show some form of identification and provide his or her name and the name and contact details of the sender. In rural areas, where people may not have government-issued identification, the deliverer relies on his or her knowledge of the community and customers. Agents sometimes deliver money to the same people on a

monthly basis over many years. If the recipient is unknown and does not have identification, the agent will typically ask a local elder to vouch for the recipient's identity.³⁵

The obligation of MTOs and agents to confirm that the legitimate beneficiary has retrieved the funds reassures the consumer that the transaction has been completed and the money has not fallen into the wrong hands. Agents rely on their social capital within their communities, their knowledge of local customers, and name-matching and pattern recognition techniques to ensure that money is reaching the intended recipients. Additionally, one customer pointed out that should his family members not receive their monthly remittance, they would immediately sound the alarm and notify the MTO.

MTOS IN HUMANITARIAN RESPONSE

At a global level, the past decade has seen a steady increase in the use of cash transfer programming as a way to deliver humanitarian and development assistance—either to meet immediate needs or address longer-term livelihood issues. Cash transfers are often used as an alternative or complement to in-kind support, such as distribution of food or essential commodities.

Cash interventions were, for example, used at scale in response to the 2004 Indian Ocean tsunami. Since then, their effectiveness as a resource-transfer option has been well documented in many contexts.³⁶ In Somalia, nongovernmental organizations (NGOs) have been implementing cash interventions since at least 2003, and their use has grown exponentially in recent years.

BOX 2. WHAT IS A HAWALA?

The term *hawala*, which comes from the Arabic word for “transfer,” is often used when referring to money service businesses (MSBs) in Somalia (*xawilaad* in Somali). The term, however, usually connotes a certain degree of informality, in large part because it is a system developed to facilitate trade between distant regions where conventional banking institutions were either absent, weak, or unsafe. Hawalas predate traditional or Western banking systems, and in modern days operate in parallel to such systems. The traditional hawala in fact works by transferring money without actually moving it, often referred to as “money transfer without money movement.” Historically, such systems relied heavily on trust and honor, as opposed to any formal regulatory instruments, and debts between the sending and receiving agents were often settled through trade transactions. In Somalia, hawalas

started operating as early as the 1970s, in response to the difficulties migrant workers faced when trying to send funds to relatives. While early hawalas operated informally, over time hawala companies have had to formalize their operations and processes in order to comply with regulations in host countries, including the United States. As such, today's Somali hawalas have developed “strong anti-money laundering systems and transparency procedures to adapt to regular inspections of their records to ensure that their systems are not being used to channel support to criminal elements or conflict actors.”³⁷ As such, although MSBs in Somalia are often called hawalas, they are in fact not informal, and most are registered or licensed by the authorities in the countries in which they operate.³⁸

In most parts of Somalia, mechanisms to deliver cash that are used by aid agencies implementing cash transfer programs in other contexts (such as direct distribution, bank accounts, smart cards, post office transfers, and payments through mobile phone networks) are not available or not practical due to security. As such, the main distribution method used by aid agencies in Somalia is the MSB, often locally known as hawala.

In a humanitarian context, and particularly given the complex nature of the situation in Somalia, the advantages of using MSBs are multiple. Among other things, MSBs enable safe, quick, and cost-effective disbursement of money to

BOX 3. MOBILE MONEY TRANSFER: USING PHONES TO DELIVER AID

Despite its weak infrastructure, Somalia utilizes mobile money transfer technologies that are unavailable in many industrialized countries. As in many African countries, Somalis treat their mobile accounts as money delivery systems, sending cash from one phone to another in seconds. People in remote areas with no access to banks credit their mobile accounts to keep their money secure, make everyday purchases such as food and fuel, and even pay school fees. While this system is not yet able to support international commercial remittances, it does provide a platform for innovative, cash-based humanitarian assistance programs.

In August 2012, Oxfam partnered with local organization HIJRA and Somali mobile phone company NationLink to bring relief to needy and displaced families in Mogadishu. Beneficiaries of past cash relief programs had to wait in long lines to receive money and then travel home through insecure neighborhoods, not to mention keep significant amounts of cash in their homes and on their persons. Using mobile technologies to conduct emergency cash relief eliminated these problems. HIJRA first conducted an assessment and identified 2,090 households. Beneficiaries (most of them mothers) received a free mobile phone and were taught to use the E-Cash money transfer system. Oxfam and HIJRA then disbursed \$150 directly into the mobile accounts of the beneficiaries. Many used the cash for food and livestock, or to meet family health needs; others used it to start or support small family businesses. After receiving overwhelmingly positive feedback from program participants, Oxfam has expanded the E-Cash program to more communities in Somalia.

beneficiaries in a project area. The MSBs are also able to distribute cash without exposing agency staff or community members to the many dangers associated with traveling long distances to distribute or collect money. The MSBs are also able to distribute cash at minimal risks, reducing risks both to agency staff and to community members who do not have to travel long distances to collect their cash.

Aid agencies in Somalia would not be able to implement cash transfer programs, let alone pay staff members in the field, were it not for the MSBs. The entire humanitarian community in Somalia fully relies on the availability of MSBs to do business including transferring funds for project activities to organization staff or local partners and paying for staff and office running costs. Without MSBs, the United Nations and NGO community in Somalia would be forced to carry cash to pay day-to-day operational and program costs, placing funds and staff at risk in an insecure environment such as Somalia. Although remittances to Somalia represent a larger share of MSB transactions than international aid, cutbacks in remittances as a consequence of the global economic crisis combined with recurring droughts, conflict, and low agricultural production are likely to put increased demands on aid agencies to respond with interventions to fill gaps.³⁹

BOX 4. USING MTOS TO DELIVER HUMANITARIAN ASSISTANCE IN SOMALIA

Adeso – African Development Solutions (formerly known as Horn Relief) has been working with MSBs in the direct implementation of humanitarian programs in Somalia since 2003, when the organization established the first large-scale cash program in the country, in the Sool Plateau area of Sool and Sanaag regions. Adeso used MSBs to distribute cash grants to allow close to 98,000 people to meet their basic food and nonfood needs in a time of crisis. Since then, Adeso has expanded its delivery of humanitarian programs in the region, and to date has been able to reach nearly one million people through cash transfer programs by making use of MSBs. During the 2011 drought and famine in the Horn of Africa, Adeso used MSBs to deliver much-needed emergency cash assistance to 20,887 households (or 146,209 people) in south-central Somalia. The cash assistance helped save thousands of lives. This aid would not have been possible without the use of MSBs, as they are crucial for any Somalia-based cash program can operate.

REGULATIONS, COMPLIANCE, AND RISK

Like other MTOs operating in the US, Somali-American transfer companies face a challenging regulatory environment. They are subject to state, federal, and international regulations that seek to prevent money laundering and the financing of groups and persons designated by the US government as terrorists. Chief among the relevant laws is the 2001 USA Patriot Act, which criminalizes the financing of terrorism, requires additional customer identification procedures, mandates increased information-sharing between financial institutions and the US government, and raises the civil and criminal penalties for banks involved in channeling funds for either money laundering or terrorist financing.⁴⁰ Further, the Financial Action Task Force (FATF), which was developed by the G7 countries to combat the illegal use of the international financial system, has issued 40 additional Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) regulations.⁴¹

Somali-American MTOs also face unique regulatory challenges stemming from sending money to Somalia. In addition to complying with US regulations, they must navigate difficult Somali payment systems. The Central Bank of Somalia resumed operations in 2011 after a hiatus of many years, but it remains extremely weak.⁴² In the future, the Central Bank plans to establish a licensing process for remittance payers, some of which may develop into full-fledged, certified commercial banks.⁴³

COMPLIANCE WITH US LAW

Like most remittance agencies in the United States, Somali-American MTOs seek to comply with US state and federal regulations, and they have taken significant strides in reducing risk.⁴⁴ In interviews, company leaders, regional managers, and individual agents all expressed a strong commitment to compliance. “We work so hard to follow the rules,” one agent commented.

When customers come to an MTO to make transactions, agents request valid, government-issued photo identification, such as a driver’s license, passport, or Permanent Resident Card (green card). They then enter the transactions in a computer program that screens the customer’s and recipient’s names and monitors for suspicious behavior. On average, customers send \$200-300 per month. For larger transactions, companies ask the purpose of the remittance and the source of the funds (such as the name of the sender’s employer). The transfer company keeps a record of each transaction in its computer system for monitoring by the company compliance officer. All agents and MTOs interviewed retain these records for at least five years, with a majority keeping them for more than 10 years.

All MTOs interviewed regularly screen customers against OFAC’s SDN List. The typical procedure is for agents to enter the customer’s and recipient’s names in their computer software to initiate the transaction. If there is any similarity to a match on the SDN List, the transaction is frozen and flagged to be reviewed by senior management. All MTOs reported frequent false positives, particularly for the most common names.

In addition to screening against the SDN List, companies monitor customers for suspicious behavior. If a customer makes a fuss when asked to show identification, MTO employees flag the transaction. Similarly, customers making multiple, small transactions through agencies in the same area raise concern. Many of the MTOs surveyed have weekly internal compliance meetings in which management and compliance officers screen all regional transactions, discuss any issues or suspicious behaviors that agents have reported, and draft suspicious activity reports (SARs). MTOs carry out these procedures in both the US and Somalia; in areas with no internet connectivity in Somalia, agents delay delivery until their headquarters confirm that the recipient has been checked against the SDN List.⁴⁵

A woman receives cash in Badhan, Somalia.
Daniel Gerstle / ©Adeso



TABLE 5. SOMALI MTOS AND COMPLIANCE WITH SPECIFIC US REGULATIONS

COMPLIANCE AREAS	EXTENT OF COMPLIANCE	MANNER OF COMPLIANCE	RELEVANT FEDERAL LAW
AML/CFT policy	100%	Companies create, maintain, and implement a policy	Reform and Terrorism Prevention Act of 2004
AML/CFT training for agents	100%	Companies train agents every six months on an ongoing basis	USA Patriot Act of 2001
Screening of customers	100%	Companies vet customers against the US Treasury Department's SDN List	OFAC regulations
Record keeping	100%	Companies keep records of all transactions for an average of eight years	USA Patriot Act of 2001 (requires mechanism whereby records may be made available to US law enforcement officials)
Transaction monitoring	100%	Companies monitor transactions electronically	Various AML/CFT laws and regulations
Inquire into large transactions	100%	Companies require customers to disclose the purpose and source of funds when they make large transactions. On average, the companies inquire into transactions larger than \$1,975	Bank Secrecy Act of 1970 (required maximum threshold is \$3,000)
Designated compliance staff	100%	Companies employ internal compliance officers	USA Patriot ACT of 2001

Source: Authors' interviews with CEOs, regional managers, agents and customers conducted in March 2013.

Agents of the companies surveyed receive substantive training in AML/CFT, though some MTOs conduct these trainings frequently and some only at irregular intervals.⁴⁶ The companies conduct their trainings on average every six months. One company flies agents in for a three-day compliance workshop every year. Another requires agents to go through a formal internal certification process, demonstrating their knowledge of all rules and regulations before they begin work.

These trainings all demonstrate that Somali-American MTOs devote significant time and resources to compliance with US federal and state regulations. Table 5 illustrates the compliance practices of the major Somali-American MTOs. Yet the question remains as to whether there exist any truly fail-safe methods that MTOs can adopt to prevent financial crimes.

The Somali-American MTOs devote significant time and resources to compliance with US federal and state regulations.

BOX 5. RECENT SCANDALS IN THE LARGER US MARKET FOR MONEY TRANSFERS

HSBC AND MONEY LAUNDERING

In late 2012, London-based bank HSBC was ordered to pay almost \$2 billion in fines for failing to stop criminals from using its banking systems to launder money. A Senate investigation found that it served as a “conduit for drug kingpins and rogue states,” allowing the transfer of billions of dollars to countries under international sanctions and individuals involved in criminal activities.⁴⁷

WESTERN UNION AND HUMAN SMUGGLING

Between 2003 and 2007, several Western Union agents in Arizona were found to have violated numerous AML compliance regulations by laundering money that eventually ended up in the hands of human smugglers. The company reached a \$94 million settle with the four states affected and agreed to improve its internal AML program and to cooperate with human smuggling and trafficking investigators in Arizona, California, New Mexico, and Texas.⁴⁸

There have been multiple high-profile cases in which MTOs and banks failed to prevent money laundering or the financing of terrorism. The most important prevention tool so far is greater oversight of agents by company compliance officers and leadership, including training and auditing accompanied by ongoing improvement of the software platforms utilized to detect suspicious activity. As the cases in Box 5 suggest, several major MTOs and banks have not succeeded in establishing fail-safe transfer procedures.

REGULATIONS AND RISK: ACCOUNT CLOSING EXPERIENCES

Over the past 10 years, Somali-American MTOs in the United States have struggled to find banks willing to host their accounts. By the late 2000s, with most major banks unwilling to facilitate remittances to Somalia, most Somali-American MTOs had opened accounts with Sunrise Community Banks, a small financial institution based in Minneapolis. In December 2011, in the wake of two high-profile prosecutions of Somali-Americans in Minnesota, Sunrise decided to close Somali-American MTO accounts, leaving the MTOs scrambling to find alternatives. They have had minimal success. One MTO executive reported that only a single bank continued to work with the business. If this bank were to close its accounts, the MTO would “almost certainly be forced out of business.” Another MTO representative spoke of approaching a new bank about opening an account; bank staff refused to meet with him, and when he persisted, he was told that he was “wasting [his] time.”

BANK LIABILITY

US legislation, including the Bank Secrecy Act and the USA Patriot Act, requires financial institutions in the US to assist federal government agencies in detecting and preventing money laundering and terrorism.⁴⁹ If financial institutions fail to do so, the US Treasury Department’s Financial Crimes Enforcement Network (FinCEN) and other regulatory agencies can impose multibillion-dollar monetary penalties and/or terminate the institutions’ operating licenses.⁵⁰ Banks and other financial institutions are not legally responsible for their clients’ actions, per se, but they are responsible for exercising due diligence with regards to AML/CFT. Some banks, overwhelmed by the task, simply choose not to work with clients whom they perceive as risky.

BANKS ALARMED BY INCIDENTS OF MATERIAL SUPPORT

In addition to feeling the weight of their responsibilities and liabilities, banks perceive a heightened risk in dealing with Somali-American money transfer businesses. In particular,

BOX 6. AN EXAMPLE OF BEST PRACTICES

In this difficult climate, it is important to highlight cases in which banks evaluate Somali MTOs on the basis of a fair assessment of their risk mitigation strategies. In April 2013, several articles in the press reported discussions between Dahabshiil and U.S. Bank. According to a U.S. Bank spokesperson, “We are pleased that we may have recently found a solution with one remitter-Dahabshiil. Although it has taken us some time to get through this process given the complexity of the issues and regulations, we expedited our approval and monitoring to the full extent possible. We are currently in discussions with this remitter to ensure all parties understand the terms and requirements necessary to allow us to properly manage the relationship. Once this occurs, we will move forward to open the bank accounts in the near future.” According to the president of Dahabshiil US, “This is a very exciting day, not only for my business and me, but also for our entire community. ... Somali Minnesotans and our families look forward to beginning to restore our lifeline.” Representative Keith Ellison, as well as Senators Al Franken and Amy Klobuchar, expressed their support for these recent developments.

The US Bank-Dahabshiil discussions constitute an important first step in ensuring a stable, regulated flow of remittances to Somalia. The fact that a major US bank has assessed the application of an individual MTO on the basis of the company’s record and current capacity suggests that, despite the challenges of sending remittances to Somalia, it is possible for MTOs to navigate these challenges in such a way that can mitigate risks and meet banks’ concerns. The discussions also create hope that other major banks will consider working with Somali MTOs. It is too soon to know, however, whether this will be a unique case or the start of a more favorable relationship between banks and Somali MTOs.

The U.S. Bank-Dahabshiil discussions, though promising, do not mean that the broader issues surrounding bank account closures and remittances to Somalia have been resolved. This development constitutes only one major bank willing to work with one Somali MTO. Moreover, Dahabshiil is one of the largest and most established of the Somali MTOs. Many smaller MTOs, which perform a similarly important remittance service, still lack adequate financial services needed to maintain the flow of remittances.⁵⁴

they note several recent incidents isolated, but alarming nonetheless—of Somali-Americans providing material support to sanctioned organizations.⁵¹

In 2001, federal investigators from the Federal Bureau of Investigation (FBI), Central Intelligence Agency (CIA), and Treasury and State departments took action against Al-Barakaat, a Somali-American MTO that they alleged to have channeled funds to an armed group in Somalia. After shutting down operations and seizing all funds, the federal agencies proceeded through a difficult and lengthy investigation. Ultimately, FBI agents reported that the available evidence left them with many suspicions, but no direct, unequivocal link.⁵²

Throughout the 2000s, the US government has carried out occasional investigations of Somali-American remittance companies and agents. In 2008, four Somali-American men were arrested for channeling \$8,000 to a sanctioned armed group in Somalia. One of the men, Issa Doreh, worked at a Somali-American MTO, Shiidal Express, in San Diego.⁵³ On February 22, 2013, a federal jury convicted these men of conspiring to provide material support to a terrorist organization. According to FBI Special Agent Daphne Hearn,

“While the FBI is not concerned with the legal transfer of funds to family, friends, and charities overseas, when individuals provide material support to designated terrorists or terrorist organizations, the FBI and our Joint Terrorism Task Force partners will bring all resources to bear, to investigate these plots with a common goal of protecting all Americans from those who wish to do us harm.”⁵⁵

In April 2009, the FBI obtained warrants to search three MTOs in Minneapolis. The bureau reportedly spent five hours going over customer lists and transaction records. FBI agents did not specify what they were looking for, but some sources speculated that it was related to the recruitment of Somali-American youth in the Twin Cities by Somali armed groups.⁵⁶ The MTOs cooperated fully, and the raids did not lead to any charges or arrests. However, MTO agents expressed concern that incidents such as these would ruin their reputation in the community, creating a false impression that they did support terrorist groups.⁵⁷

The Somali-American community has made it clear that the isolated incidents of a small number of Somali-Americans are not representative of the beliefs and values of the community

as a whole. One Somali-American MTO customer emphasized: “We care about American security very much. We don’t want any funds to finance terrorism.” Nonetheless, the incidents have created a perception among banks and the general public that money transfers to Somalia are fraught with risk.

ACCOUNT CLOSURES

As a consequence of this perception, many banks refuse to work with Somali-American MTOs. On average, the Somali MTOs interviewed have experienced 19 bank account closures since the early 2000s. Among MTOs, they are not alone in experiencing closures. However, interviews with five Latin American MTOs found that they experienced on average 10 bank account closures during the same period. These figures would suggest that Somali-American MTOs may face more severe difficulties in finding banks willing to work with them.

BANKS DO NOT PROVIDE REASONS FOR CLOSING MTO ACCOUNTS

In closing the accounts of Somali-American MTOs, banks appear to be acting out of general aversion to risk rather than to any specific concerns regarding their compliance practices. Many MTOs were willing to share account closure notifications that they had received. The notifications were extremely general, typically mentioning bank policies against high-risk accounts. One MTO executive shared that none of the 40 account closure and rejection letters he had received mentioned any wrongdoing on the part of his company.

BETWEEN COMPLIANCE AND RISK: ASSESSING THE GAPS

This report finds that Somali-American MTOs generally comply with regulations and eagerly seek to minimize the risks associated with their business. However, it is clear that MTOs could improve their approach to risk management in three ways. First of all, because agents typically know customers very well, they may sometimes treat the checking of identification with a degree of informality. According to our interviews, 90 percent of Somali-American MTOs have a policy of checking identification without exception, but the remaining 10 percent admit occasional lapses into informality with customers whom they know well, or with customers who come in to make very small transactions. Ensuring that 100 percent are asked for government-issued ID would greatly reassure banks.

Second, though most Somali-American MTOs have strong compliance on the outbound side of operations, they can further reduce risks on the inbound side by strengthening their relationships with agents in Somalia. Sometimes, disconnects can materialize between the US agents and their Somali counterparts. For example, one MTO admits having little knowledge about the agents working to deliver the money in

Somalia. This disconnect clearly presents some risks. For the most part, however, MTOs disconnect have already adopted policies to improve payout security. One company, for example, has a compliance team travel to Somalia yearly to meet with Somali agents and conduct an internal audit of the company’s transactions. Many MTOs have formal procedures for selecting agents, including background checks and checks against the SDN List.

Third, and largely beyond the MTOs’ control, the payment system in Somalia makes tracking funds very difficult. In other countries, MTOs typically regulate payments from the origin. On the payout side, central banks generally have policies requiring payers to document the legality of the transfer. Though regulators may audit payers only infrequently, they do monitor the process and perform surprise visits to make sure that everything is in order.

However, the federal government of Somalia currently does not regulate payment systems. In an interview, one US federal regulator mentioned that compliance issues lie not with Somali-American MTOs, who are “doing the best that they can,” but rather with oversight of payments in Somalia. Currently, the Central Bank of Somalia does not license payers or keep any official records of this sort. Thus, it is difficult for US federal regulators to trace money transferred to Somalia. In fact, they often are unable to trace money past MTO clearinghouses in Dubai or to ascertain its destination in parts of Somalia. This last and most serious gap can only be filled by creating secure mechanisms for payments in Somalia through gradual improvements in Somali government regulation, enforcement, and transparency.

These areas of risk deserve greater attention on the part of MTOs and agents. However, US banks have responded in a manner disproportionate to the level of risk involved and have failed to distinguish among Somali-American MTOs, treating companies that are meticulous in their policies and practices in the same way that they treat those that take a less rigorous approach.

US banks have responded in a manner disproportionate to the level of risk involved and have failed to distinguish among Somali-American MTOs.

IMPACT OF ACCOUNT CLOSURES

Account closures began to affect Somali-American MTOs as early as the 1990s and spiked in the years following the attacks on the World Trade Center and Pentagon in 2001. MTOs operating in Minnesota seem to have felt the largest impact, although account closures have affected companies operating in other states as well. These closures have disrupted an economic lifeline to Somalia, hindered business growth, encouraged informality among remittance senders, and strained relations between the Somali-American community and US officials.

DISRUPTION OF INCOME IN SOMALIA

By far the most significant and direct impact of account closures was the interruption in money transfers to Somalia after Sunrise decided to close Somali-American MTO accounts at the end of 2011. Most companies interviewed reported delays ranging from several weeks to several months before they could locate a new bank and begin sending transfers again. One Minneapolis taxi driver described how, for over a month in early 2012, he could not send money to his wife and children. Another customer described how a young man in his family dropped out of school when remittances were interrupted. “The blockade was difficult for every Somali family,” a community leader in the Minneapolis area declared. He recalled that Somali-American MTOs were “desperately” contacting banks and financial institutions to find a way to keep remittances flowing. And he asserted that the Somali-American community’s main concern was the possibility that remittances would be permanently cut off. Overall, most MTOs said that the volume and amount of transactions that they have processed have fallen since late 2011 as a consequence of interruptions in remittance flows, the rising cost of transfers, and an increase in informality—all directly or indirectly caused by account closures.

Everyone interviewed for this study agreed that if account closures were to cut off remittances to Somalia, the impact would be devastating.

Many Somali-American interviewees also expressed the desire to increase their investment in businesses and development within Somalia, but account closures have threatened to create a bottleneck of money transfers that delay and even discourage investment in the country.

Everyone interviewed for this study agreed that if account closures were to cut off remittances to Somalia, the impact would be devastating. In the words of one MTO manager, it would be “a huge humanitarian crisis.” At present, without concerted effort by MTOs, banks, and the US government, the risk of a remittance cutoff looms large.

BUSINESS PERFORMANCE

The bank account closures have severely impacted Somali-American MTOs, limiting their opportunities for further business expansion and development. Almost all MTOs had most—if not all—of their local bank accounts closed. As a result, they spent significant time and resources looking elsewhere—including out of state—to find banks that were willing to do business with them.⁵⁸ On average, Somali-American MTOs currently have accounts in one to two banks.



Money to be distributed through Adeso's cash relief program in Badhan, Somalia.
Daniel Gerstle / ©Adeso

On average, Somali-American MTOs currently have accounts in one to two banks.

Several companies indicated that they had initially anticipated expanding into states outside of Minnesota, including Ohio and Washington, to serve Ethiopian, Kenyan, and other East African communities. The bank account closures forced them to re-evaluate their plans for expansion and concentrate on responding to the immediate need to find a small number of banks to facilitate transfers to Somalia.

The level of risk facing these companies has also increased. With a large amount of funds distributed across fewer banks, many MTOs have assets in bank accounts in excess of the Federal Deposit Insurance Corporation (FDIC) standard insurance amount of \$250,000 per depositor, which exposes companies and their customers to risk. One company had more than \$1 million in one bank account. Transferring these funds also presents risks; several MTOs have resorted to renting armored vehicles to transport cash from their main offices to banks in other states.

INCREASED COSTS

Account closures have greatly affected the companies' operating costs and subsequent profit margins. The cost of hiring armored vehicles to transport cash to out-of-state banks is significant; one individual indicated that his company spends approximately \$1,200 a month to transport money twice a week to banks in three different states. Additionally, smaller banks tend to charge more in various fees and are generally less efficient. One company indicated that one of its small banks charges 25 cents for every \$100 deposited, substantially cutting into his business's revenues.

Following the 2011 Sunrise account closures, customers began sending money through more expensive and indirect corridors. One agent described how some of his customers had tried using Western Union to send money to Kenya, and then another MTO to transport the remittances into Somalia. A community leader recalled how some Somali-Americans sent money first to the Middle East and then had it transmitted from there to Somalia. This strategy essentially doubled their cost of remitting, as they had to pay two commissions on the transaction.

Rising bank fees and added costs will most likely lead to higher prices for transferring money. Although most MTOs interviewed have tried to resist raising their rates, it is almost inevitable that these costs will eventually be passed down to their customers in the US and recipients in Somalia.

INFORMALITY

As Somali-Americans' access to formal MTOs becomes increasingly restricted, the risk that they may turn to other, more informal mechanisms for transferring money increases. This shift already occurred in the immediate aftermath of the account closures; as MTOs scrambled to find other bank accounts, several agents and customers attested that many Somali-Americans sent money home via family or other travelers.

In addition, it would reduce the transparency of transactions and compromise the ability of the US government and Somali authorities to monitor and regulate the transfer of funds.

Remittances to Somalia will not stop with a complete shutdown of MTO bank accounts, even if many companies go out of business. In the event of further bank account closures, Somali-Americans will send money nearly exclusively through informal channels, which further increases the cost and risk of remitting. In addition, it reduces the transparency of transactions and compromises the ability of the US government and Somali authorities to monitor and regulate the transfer of funds.

EROSION OF TRUST AND COMMUNITY RELATIONS

Many MTOs, community organizations, and customers described feeling unfairly targeted because of their nationality. "This is discrimination," one community leader said bluntly. "We thought that the US was a country that always welcomes immigrants," one customer commented. Many of those interviewed described two sources of friction: first, a sense of frustration with US financial regulators for failing to ensure a secure channel for remittances, and second, a sense of exclusion from US banking institutions based on their nationality.

Banks appear to have a preconceived notion of the risk associated with Somali MTOs, regardless of company AML/CFT practices or leadership, based on the destination of the remittances.

With several recent, high-profile prosecutions of Somalis for providing material support to armed groups opposing the government, many in the community are concerned with how they and their homeland are being portrayed in the media and how they are perceived by those outside the community. In one interview, a Somali-American described wanting to explain to Americans that Somalia is more than just armed violence.

Bank account closures have exacerbated the situation, creating frustration with US officials among those in the Somali community. One individual described this as "creating a wedge between the US government and Somali-Americans" by fomenting feelings of distrust.

The account closures have also created a wedge between the Somali community and several of the banking institutions. Many of those interviewed expressed frustration with the way that their companies—and by extension, their community—were treated. "It's bias," said one agent. Some noted that they understood why small banks chose not to withstand the regulatory scrutiny that comes with working with Somali-American MTOs, reserving their frustration for larger banks that would be well equipped to handle complex and challenging regulatory situations. "For them, it's small potatoes, but for us, it's how we feed our families," one customer noted.

Relations with certain banks further soured when they reportedly closed the personal accounts of the owners and agents along with the business accounts. According to interviews, Somali-Americans who may have worked with an MTO in the past but currently do not were also blocked from opening personal accounts at these banks for the future. This policy even extended to individuals who had indirect relationships with MTO owners and agents; in one instance, a partner in an unrelated business venture had his account closed. In most cases, individuals received little to no explanation of the reason behind their personal account closures; letters from the bank simply stated that bank policy required it. These personal account closures contribute to the Somali-American community's sense that it is being singled out.

A woman receives cash relief from Adeso through a Money Transfer Operator in Badhan, Somalia. *Daniel Gerstle / ©Adeso*



Notwithstanding these sentiments, we did not find evidence that banks or regulators singled out Somali-American MTOs because of a distrust of the Somali-American community. However, we did observe that banks appear to have a preconceived notion of the risk associated with Somali MTOs, regardless of company AML/CFT practices or leadership, based on the destination of the remittances. Even though we do not believe that banks are discriminating against Somali-Americans, it is no wonder that their unwillingness to even consider working with Somali-American MTOs fuels the widespread impression that they are singling out the Somali community.

Although many in the Somali community are frustrated, they have not given up hope that the US government can help them. They described feeling supported by their elected officials, many of whom had spent significant time discussing the importance of money transfers with them and developing potential solutions.

RECOMMENDATIONS

Our main findings confirm the crucial role of Somali-American MTOs in Somali communities. It is essential for Somalia's immediate survival and long-term development that MTOs continue to operate in the US and that they freely and securely transfer money from Somali migrants to Somalia. With a concerted effort from all sides, it is possible to achieve this goal without compromising the US government's security imperatives or banks' business interests.

BANKS SHOULD EXPAND SERVICE TO SOMALI-AMERICAN MTOS

Banks should take the initiative to identify ways to safely facilitate money transfers for Somali-American communities. Sending money to Somalia presents risks to banks, but these risks are neither unique nor insurmountable. Somali-American MTOs are taking significant steps to ensure that their transactions are safe and legal. Although banks enjoy freedom of contract to open accounts for clients of their choosing, their collective record of summary MTO account closures without explanation and refusal to consider the merits of MTO account applications suggest that their decisions are guided more by preconceived notions of risk than by actual risk. Greater efforts by banks to evaluate Somali-American MTOs applications on a case-by-case basis will lead to expansions in service for Somalis without a meaningful increase in the banks' own reputational or legal exposure.

US POLICYMAKERS SHOULD PRIORITIZE REMITTANCES TO SOMALIA

Remittances to Somalia account for a significant percentage of Somalia's GDP and play an integral role in its development. The international community has devoted a great deal of money and attention to enhancing security, building public institutions, supporting economic development, and carrying out

humanitarian response. Maintaining an open, secure channel for Somali migrants to invest in Somali communities and send money to their friends and families must rank as highly as any of these priorities. A remittance channel closure is among the most worrisome of the possible and foreseeable catastrophes that could befall Somalia in the future; even a partial shutdown could cause tremendous economic and social trauma, pushing money transfers toward informality and threatening the country's progress toward peace, security, and sustainable development.

US Treasury Department officials, particularly in the Office of the Comptroller of the Currency (OCC), should build their understanding of Somali-American MTO compliance practices and encourage banks to open accounts for responsible companies. State Department officials and National Security staff covering Somalia should prioritize remittances and develop contingency plans for shutdowns and reductions in service, bearing in mind that increases in aid are not an adequate substitute for the sort of direct financial flows from diaspora communities that build resilience and track people's needs and priorities directly.

THE US TREASURY DEPARTMENT SHOULD HELP INTEGRATE SOMALI-AMERICAN MTOS INTO AN AUTOMATED CLEARINGHOUSE (ACH)

Most Somali-American MTOs currently process transaction information through clearinghouses in Dubai before local agents are authorized to deliver funds. The money is then passed on to local agents, who are responsible for ensuring that the funds are delivered or transferred to the intended recipient. The US Treasury Department can bolster the security of the remittance system by facilitating the creation of a shared clearinghouse based in the US; many MTOs expressed support for such a move. The clearinghouse would aggregate all transactions originating from all MTOs and agents, thereby helping regulators and MTOs identify remitters sending funds through multiple MTOs to avoid

scrutiny. It would minimize redundancies, enhance oversight of local agents, and improve compliance with US sanctions regimes. The clearinghouse should be jointly financed by the Treasury Department, banks, and MTOs.

MTOS SHOULD IMPROVE TRAINING AND MONITORING OF AGENTS

Agents in both the origin and the destination country of the remittance are key conduits in the transfer of money. They are best positioned to identify and prevent potential violations of US law during money transfers. Therefore, MTOs should continue to provide agents with diverse and appropriate methods of training to detect suspicious activities. MTOs should also regularly test their agents' performance, keep documentation of all trainings and tests at their headquarters and regional offices, and carry out regular site visits and performance tests. In particular, MTOs must take steps to improve communications with and oversight by Somali agents and contractors to ensure secure remittance deliveries.

MTOS AND REGULATORS SHOULD COLLABORATE ON BEST PRACTICES

US state and federal regulators should cooperate with the money transfer industry to create a series of standards for responsible money transfer operations. Although this framework would be useful for all MTOs, it is particularly needed by Somali-American companies. In addition to promoting a set of uniform compliance policies and procedures, it would help rehabilitate the image of MTOs in the US by directly addressing the fears and negative perceptions held by some banks.

Industry best practices would specify appropriate standards for training, licensing, and formal auditing. They would also include specific guidelines for monitoring MT0 agents within Somalia, in order to establish a certification and licensing system. Some Somali-American MT0s have already taken these steps, but they have failed to change the perception of US banks and regulators.

MTOS SHOULD DEVELOP MOBILE MONEY TRANSFER TECHNOLOGY FOR SOMALIA

Telecommunications is a fast-growing sector in Somalia. At least three Somali mobile network providers have developed money transfer platforms. Somalis are already using mobile technology to pay for goods and services. Aid agencies have found mobile money transfer to be an attractive option due to reduced leakage, improved reconciliation and control of expenditure, greater speed and efficiency of transfers, and reduced costs.⁵⁹ Mobile money delivery also offers the opportunity for real-time tracking of payments.

Many MT0s expressed a desire to utilize this technology to facilitate international money transfers through a platform like M-Pesa in Kenya. In order to do so, they will have to navigate federal and state regulations in the US, coordinate with Somali

authorities, and encourage cooperation between multiple private sector interests. Somalia is a viable market for international mobile money transfers.

THE US GOVERNMENT SHOULD HELP SOMALIA REGULATE ITS PAYMENT SYSTEMS

Through technical assistance and capacity building, the US government can greatly help Somalia improve its payment system infrastructure. For example, the US government could help the Somali Central Bank monitor compliance could assist with the drafting and enactment of licensing requirements, and could facilitate the development of benchmarks for money laundering prevention.

SOMALI AUTHORITIES SHOULD ACTIVELY REGULATE INTERNATIONAL MONEY TRANSFERS

In order to build confidence and encourage US Treasury Department support, Somali authorities and the Somali Central Bank should demonstrate their serious commitment to AML/CFT by passing regulations and actively responding to the concerns expressed by international partners.

ACCOUNT CLOSURE LETTER FROM A SMALL BANK TO A SOMALI-AMERICAN MTO

RE: [REDACTED] Your Deposit Account Relationship with

Dear

We have recently completed a review of your account and determined we are unable to continue our banking relationship with you. We acknowledge that you have banked with us for a number of years, however, trends in the regulatory environment and changes in our Bank's policies require that we discontinue your relationship.

In order to provide time for you to relocate your accounts, we are not closing them immediately. Instead, we would ask that your accounts be closed no later than SEPTEMBER 20, 2012. Any collected funds remaining in your accounts on SEPTEMBER 20, 2012, will be sent to you at the address we have on file for mailing account statements and notices, via the United States Postal Service in the form of a cashier's check. No deposits or withdrawals will be processed beginning on this date.

Our goal is to assist you in the orderly closure of your accounts and would ask that you call me with any questions that you may have in this process. I can be reached at [REDACTED]

Sincerely,



APPENDIX 2

ACCOUNT APPLICATION DENIAL LETTER FROM A LARGE BANK TO A SOMALI-AMERICAN MTO

[REDACTED]

[REDACTED]

August 1, 2012

Reference #: [REDACTED]

Dear Business owner:

Thank you for your [REDACTED] business checking or savings account application. The Office of the Comptroller of the Currency (OCC) has issued guidance regarding factors that a national bank should consider when evaluating a new account request for a Money Services Business. Our analysis of the information received leads us to conclude that your business did not fall within the acceptable risk parameters of our Money Services Business Program as a result of at least one of the following:

- o Your company did not meet our requirements in our business due diligence background investigation.
- o [REDACTED] determined that your account(s) create an unacceptable level of risk for the bank.
- o The [REDACTED] Money Services Business Due Diligence Unit did not receive requested information by the required date.

This letter confirms that your account application is declined.

Again, thank you for your interest in doing business with [REDACTED]

Thank you.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

APPENDIX 3

MAP OF SOMALIA



Source: United Nations Office for Coordination of Humanitarian Affairs, Somalia (2013).

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COVER : A woman uses cash transferred through a money transfer operator to buy goods in Kulmiye, Somalia. *Daniel Gerstle* / ©Adeso

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