Global Remittances: Update on the UK-Somali Corridor

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I. Introduction

In May 2013 Barclays Bank in the UK announced it was shutting down the accounts of four Somali Money Service Businesses (MSBs) including Dahabshiil, the largest remittance company operating in the Somali regions. Following international uproar, and a Somali diaspora-led grassroots campaign, the UK government took on the task of setting up an Action Group on Cross Border Remittances and a Somali-UK Safer Corridor Pilot Project with the aim of finding a durable solution to the problem. Two years later, however, the Safer Corridor Project has collapsed. Legal remittance flows persist, albeit in a fragile and precarious environment. This paper provides a brief update on the Safer Corridor Initiative, its challenges, and how the money transfer sector has been adapting to the process.[1]

II. De-Banking

Over the last few years, mounting pressure from international financial regulators and policy makers (particularly in the US and the UK) has led to tighter regulation around the prevention of money laundering (Anti-money laundering, AML) and the financing of terrorist activities (Counter-terrorist financing, CFT). The post 9/11 financial war on terror has meant that banks are expected to abide by Know Your Customer (KYC) regulations, and are held accountable if their customers are financing terrorism-related activities or money launder-

ing. For example, in 2012 HSBC was fined $1.9 billion by US authorities for money laundering offences and lack of controls, and as a result closed down its MSB accounts. These changes have been part of a wholesale de-risking and de-banking approach, which has more recently impacted on the Muslim charity sector in the UK. In 2014, the accounts of various Muslim organisations, including Finsbury Park Mosque and the Cordoba Foundation, were closed. Concerns with regulation have meant that access to financial services has become increasingly discriminatory, based on perceptions rather than factual information about the organisations and the countries affected. Muslim organisations, or those linked to unstable, developing countries or those with a presence of terrorist groups, such as Somalia, have been unduly affected. This tightening regulation around financial flows has not been confined to the UK and the US. Earlier this year, the Kenyan government also shut down the accounts of 13 Somali remittance companies suspected of financing terrorism following al Shabaab's attack at Garrissa University where 148 students were killed.[2]

It is within this global climate that on the 8th May 2013 Barclays Bank in the UK announced that it planned to shut down the accounts of 250 MSBs. These closures included four Somali MSBs operating in the UK: Dahabshiil (the largest in the Somali remittance market and a major player in the formal economy of the Somali regions), Mustaqbal, Tawakal and Horyaal. This decision came as a result of Barclays Bank weighing up the perceived risks and due diligence costs against the profitability of banking MSBs.[3] The MSB sector has historically been perceived as risky by banks and regulatory authorities, and banks came to realise that the fines associated with non compliance with AML and CTF were seen to outweigh the benefits of providing accounts to MSBs.

This has had severe repercussions on the Somali financial sector. There are no internationally recognised banks in the region, and only a very fragile central banking system exists. Consequently, Somali MSBs are responsible for sending over 1.2 billion USD to the Somali regions, more than international aid, foreign investment and exports together.[4] Furthermore, the system is crucial for providing financial services and for linking the unbanked with the banked sectors of the population. It is considered to be cost efficient in contrast to large remittance companies such as MoneyGram and Western Union which are not well represented across the Somali regions and charge considerably more than most Somali MSBs.[5] Aside from WorldRemit,[6] which operates online,

all remittance companies lost their banking accounts in September 2013 as Barclays was the last bank to offer accounts to MSBs in the UK. As evidence by Oxfam reports, these closures constituted a significant threat to the Somali lifeline.[7]

III. The Safer Corridor Pilot

Whilst the UK government was initially reluctant to intervene—citing the problem as a 'commercial' one over which they had little control—this changed following a 2013 campaign which saw Somali community activists working alongside academics and NGOs (Oxfam and Adeso). In October 2013, the government committed to setting up an Action Group on Cross Border Remittances composed of three working groups, one of which was in charge of designing and implementing the *Safer Corridor Pilot Project for UK-Somali remittances*. The advisory group overseeing the project included SOMSA, community representatives, banks, regulators, NGOs, international partners and the UK and Somali governments.

The Safer Corridor Pilot was set up to create "a more transparent and safer system for Somalis in the UK to send money back home."[8] It aimed to ensure that flows to the Somali regions remained in place, creating an effective regulatory framework to address banks' concerns, while enabling them to re-establish business relations with credible MSBs. In doing so it sought to initiate various interventions throughout the process of remittances flow—from sender to receiver—thus addressing security and compliance risks. The UK Department for International Development (DfID) was the lead department tasked with funding the project and bringing relevant stakeholders together, while the World Bank was responsible for the design and implementation of the project. Consult Hyperion were commissioned by the World Bank to undertake research in the Somali regions, which was outsourced to another consultancy firm called Katuni. They conducted a small sample survey in the Somali cities of Galkayo, Hargeysa and Borama. This consultancy was one of many projects commissioned by the World Bank and DfID throughout the duration of the Action Group and Safer Corridor project.[9] Consultancy after consultancy nonetheless failed to provide any tangible results.

One of the prevailing issues to emerge early on in the project was the necessity of persuading banks to take ownership of the project. While DfID provided a number of guidelines on compliance for MSBs,[10] and

arranged meetings and discussion groups aimed at persuading banks to take on remittance accounts, they could not assure banks they would not be fined should an AML or CFT issue arise. All DfID could do was improve the perceptions of risk, and support MSBs in strengthening their compliance procedures. They could not ultimately guarantee that banks which opened accounts for compliant MSBs would be exempt from incurring fines if these companies were subsequently found to be engaged in financial terrorism or money laundering related activities.

A second major concern was the proposed idea of the Third Trusted Party. Consult Hyperion envisaged that the data of transactions from the UK to Somalia/Somaliland would be stored and managed by a Third Trusted Party. However, issues relating to the nature of the proposed entity, its location and precise function remained unclear. During the numerous consultations and community engagements, MSBs and Somali members of the public raised concerns around data protection, privacy, and other security issues.

During our interviews with MSBs, directors commented on a felt sense of injustice and unnecessary suspicion when it came to their operational procedures and systems. An environment of distrust, they explained, had generated suspicion between MSBs and others tasked to address and improve the situation. Further confusion existed about what precisely was required of MSBs in order to qualify for a bank account. There seemed to be a certain level of frustration with the perceived lack of direction and the slow pace of developments around the project.

In early 2015, after several delays in the timeline of the project, issues emerged in relation to the management of the project by the World Bank. Due to yet unknown circumstances the Safer Corridor project ceased. Two years later, it remains unclear whether the pilot will be ever completed. The UK government has now shifted to a more medium-long term Safer Corridor Initiative, which will address the structural flows of remittance flows working closely with the Central Bank of Somalia and the Federal Government of Somalia.[11] The US State Department has more recently taken control over the management of the Safer Corridor project and released a Request for Interest to capacity build Somali financial institutions including the Central Bank of Somalia and Somali MSBs in the Somali regions. The US Treasury is now leading the project, but further clarity and details of this initiative are still pending.

A. Remittance Flows Continue

Meanwhile, all MSBs with the exception of Word Remit, have now lost their bank accounts in the UK. Prior to the bank account closures there were three different ways (or transfer channels) to send money via MSBs. The first, which is also the most common method used, involves individuals sending money via their local agents, either in cash or through digital transaction. Local agents then transfer the cash to the MSBs' specific bank accounts. The second is used when senders take the money directly to the MSB's own office and pay in cash over the counter, and the third involves the transfer the money from the sender's bank to the MSB's bank account.[12] In all three channels once the MSBs receive the money in their accounts, it is transferred to a clearing house, often in Dubai, and subsequently to Somalia or Somaliland. These transfers are typically categorised into three miles. The *first mile* involves agents depositing monies into an account of a UK MSB, which then the MSB then transfers to a third party clearing house, often based in the UAE. The *second mile* involves the settling of payments using trade-flow mechanisms to reimburse in-country agents, and the *third mile* takes place in the Somali regions where the local agent receives the payments to settle.[13]

The process of transferring money has been complicated since the closure of MSB bank accounts, as MSBs have struggled to offer transfer services for individual senders. In order to address this challenge, MSBs have opted to work with a third party, for example MoneyCorp or Choice,[14] to collect the cash once senders deposit it with the local agent. To complicate matters more, such third parties are offering partial services and are not willing to collect the cash from the agents but instead insist that MSBs arrange a central collection point. This presents added labour costs due to physical cash collection but also real and immediate risks to MSBs, their employees and the industry as a whole. Thus far, business transactions are largely unaffected because the Bank of Abu Dhabi has agreed to accommodate such transactions but this may well change in the near future. Furthermore, there is the possibility that intermediaries such as MoneyCorp and Choice may be forced to end collaboration with MSBs if the situation in the Somali money transfer industry does not improve.

Companies such as MoneyCorp, which provide similar services to Somali MSBs, are fully operating in the UK, and have not been subject to the restrictions affecting Somali MSBs. Questions have been

raised by community leaders about what they perceive as unequal access to banking services. For example, Mohamed Ibrahim, Director of the London Somali Youth Forum stated, "We sense unfairness in how Somali people are treated by banks who view them as suspicious and untrustworthy that is evident in the massive account closures while other organisations who handle in the same exact industry are operating freely. Can we speak of racism here?" The sense of unfair treatment was also expressed by the SOMSA chairman who noted that "the reality is that we are of course losing great market share due to the closure of our bank accounts only to be picked up by rival orgnisations." Despite these challenges remittance flows to the Somali regions continue, albeit in a way that is less transparent and, inadvertently, can more easily facilitate money laundering and terrorism-related activities.

IV. Regulatory Challenges

Our research has shown that MSBs at the *first mile* demonstrate a greater understanding of the requirements and risks at stake, particularly owners and senior staff members in the UK, UAE and USA. Most suggest that their current money transfer IT systems are not conducive to acceptable standards that meet the demands of financial regulators and compliance and financial procedures. As one senior MSB manager pointed out to us, most technical money transfer systems "are built in-house by our own IT engineers and, therefore, most violations are to do with the security aspects of the systems." However, he also reiterated a commitment to improve the services through innovative solutions which meet regulatory obligations. This might involve, for example, moving the MSB online (ecommerce) and dealing with operational requirements of any new IT system that is adopted, (i.e. disaster recovery, high availability, system performance, usability etc.). That said, many MSBs indicated the need for guidance and training in order to meet the demands of acquiring and using technical solutions that comply with required international compliance and procedures. Arguably, the Somali remittances industry has been slow in working collaboratively or in offering training and guidance. Indeed, current challenges have existed for more than a decade.

Regulators are particularly concerned about the physical transportation of large amounts of cash between the second and the third miles. Continuous transportation of physical cash takes place at least twice a

week from various parts of the Somali regions to Dubai and vice versa—a process which lacks transparency. The cash is carried with cabin size bags to and from Dubai to meet the supply and demand of cash flow. Due to the fact that the banks treat this money, albeit legally, as foreign exchange transactions, profits of up to 2 per cent can ensue in the transfer from US Dollar to UAE Dirham. This makes it an attractive financial activity.

Finally, compliance regulations are of greatest concern in the *last mile*. The traditional *kafaala* system (identification through clan membership) is still widely used as a credible form of identification. This means if someone cannot be formerly identified during remittances collection, s/he needs to bring a well known and/or respected clan elder to vouch for her/him. Only those with foreign Passports (i.e. Djiboutian, Ethiopian, European, American etc.) are readily identified. In the absence of formal identification, community contacts and clan-based identification systems remain the most reliable means of identifying individuals. However, this system has little credibility with Western banks and international law-enforcement agencies. In late 2014 the Somaliland government started to implement national ID cards, which could also be used for identification purposes. However, this project is still far from completion. This underpins the concerns of international regulators in terms of KYC and AML as there are virtually no effective KYC procedures in place. While aggregated cross transactions checks are performed in order to monitor individual behaviour when transferring—thus enabling MSBs to identify any 'suspicious' transactions—the actual identity of the receiver is harder to ascertain.

V. State-owned and Newly Emerging Private Banks

Poorly functioning public financial institutions and weak governance are major constrains for the MSB sector. The central banking systems in Somalia and Somaliland are not developed enough to undertake supervisory roles of monitoring the MSB system. The Somaliland Central Bank has only recently introduced a Supervisory Unit with some capacity training provided by the World Bank. As in other sectors, however, state institutions are far less developed than the private sector, which has flourished despite political instability in the region. A power disparity exists between the private sector and government institutions in Somaliland. Often private organisations make sugges-

tions to regulate their own industry and the government abides by this, thereby blurring accountability.

Meanwhile, the remittance market has been developing in the Somali regions. Over the last few years, we have seen the emergence of private banking institutions operating in the area. Salaam Bank opened in 2009 and offers current accounts, ATM machines, web surfer cards (prepaid), and limited credit. Dahabshiil Bank opened in late 2014, offering general banking services including both current and business accounts. These banks issue cheques, some of which are interchangeable between these institutions. Although not internationally recognised, due to the lack of a centralised banking system, some of these banks can perform international transfers through recognised corresponding banks (E.g. Salaam African Bank in Djibouti). These transactions are, however, slow and expensive. Some have been working towards providing a swift system, but this has not yet materialised. Furthermore, these banks tend to service businesses but are less likely to service NGOs or individuals, due to the high costs involved, and the fact that remittance companies offer similar and cheaper services. All banks currently operating in Somaliland have been awarded Sharia-compliant licenses, in the absence of a commercial banking law in the country.

These licenses enable them to offer a wide range of services in order to meet the increasing local demand. Central to the Sharia based banking is the absence of interest charges on economic transactions and a duty to avoid reckless risk-taking.

A key development of the last few years has been the expansion of mobile money systems such as ZAAD and E-Dahab in Somaliland, EVC Plus in South Central Somalia, Sahal in Puntland, as well as the more recently established Taaj. These companies currently present a huge threat to the existence of traditional remittance business models described above. Mobile money is becoming increasingly entrenched across the Somali regions, especially in urban areas and among younger generations. Many recipients of remittances are now accustomed to mobile money and that service is currently solely controlled by telcos such as Telesom, Gollis and Hormood. There have also been connections between MSBs, Telcos and Banks. The Zaad system, for example, is a platform provided by Telesom, which also links up with Salaam Bank accounts. Money that is held in a Salaam bank account can be transferred to an individual's ZAAD mobile phone account, and vice versa. A limited number of traditional MSBs, including Mus-

taqbal and Tawakal, have also joined up with Zaad so that remitted money can be directly sent to the recipients' mobile phone. Similarly, mobile platforms EVC and Sahal are owned by companies Hormuud and Golis respectively. Telesom, Hormuud and Golis, although operating with great local independence and ownership, are linked to its pioneer and prominent shareholder Mr Ahmed Nur Jim'ale. Inspired by the large network of Mr Ahmed Nur Jim'ale, Taaj has recently penetrated the international market, enabling diaspora Somalis to directly send their money to the intended recipients across the Somali regions.

The upsurge in mobile money infrastructure and use can in great part be associated with the failure to address the challenges in the remittances industry after massive account closures by banks and the ongoing demand for money transfer services. Furthermore, mobile money services transfer money quickly, cheaply, efficiently and through transparent procedures. Having said that, greater scepticism exists about the reliability of the mobile money infrastructure among users. Local people in Somaliland use the term *ha igu dhixin* that translates as "do not [keep it on the phone] overnight." Discussions with young Somalilanders revealed their lack of trust that ZAAD money was real money. As one young female user in Somaliland explained to us, "it's just a number on my phone! How do I know it's actual money?" In sum, most people ensure that the money they receive on their phones is immediately transferred to a bank account to avoid potential loss of funds in the event of a system failure. Despite these suspicions, MSBs are beginning to realise the importance of mobile money, and are recognising the need for a mobile money platform that can compete with existing Telcos.

Another question is whether mobile money can effectively provide a substitute for traditional MSBs cash transfers. As mentioned, mobile money is widespread in urban areas and amongst youth, but less so in rural parts of the country, and among older Somalis. Those who are not able to operate a mobile phone (often older women) rely on other family members who are able to do so, charging them with the responsibility of managing their money. A final concern with the remittance closures was the extent to which the development industry, NGOs and charities working in the Somali regions, were reliant on remittance companies to process salaries to their own employees, but also to process their cash transfers to the rural poor. This continues to be a concern.

VI. Concluding Remarks and The Future

The main challenges facing the Somali money transfer industry can be largely attributed to two main factors. First, there are concerns around compliance and how to meet international financial regulations. Second, the lack of professionally operating banking systems in the Somali regions does not only exacerbate the problems but is part and parcel of the chain of critical challenges facing Somali MSBs. So what can be done and how can these challenges be addressed in the immediate and long term?

There is a need for professional, sound and well-regulated financial banking systems that meet global standards across the Somali regions. It is therefore important to aid the Central Banks of Somalia and Somaliland, in developing regulatory and supervisory mechanisms to ensure that current legislation is implemented effectively. A functioning and well-regulated financial banking system will enable proper checks and balances to be carried out through the Central Banks, which, in turn, should restore trust in the Somali financial industry as a whole. More importantly, a well-regulated banking system across the Somali regions would ensure that money laundering and the financing of terrorism are curbed.

Additionally, a Central Know Your Customer System (CKYCS) with biometric identification to meet international standards, which MSBs can share for critical identification processes, could serve as a viable option to mitigate compliance risks. Some challenges in terms of trust in relation to a shared data platform are foreseeable. These could potentially be addressed by including the Somali Money Services Association (SOMSA) in the process. Widespread scepticism about financial data management and ownership needs to be addressed in order to bring important industry stakeholders on board.

Furthermore, the physical transportation of cash to and from Dubai, while not unlawful, needs to be addressed as a matter of urgency to ensure greater transparency and accountability. A more stable centralised banking system in the Somali regions would undoubtedly rectify this.

Finally, any development towards capacity building or training should take cognisance of all three miles and their interconnections. Only by so doing can we work towards the creation of a fully functioning Safer Corridor which meets international financial regulations.

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Notes

1. This paper is based on research carried out in London, Dubai, Hargeysa, Somaliland by the authors between 2014–15. Mohamed Aden Hassan carried out three focus groups with members of Somali Money Services Associations (SOMSA) UK and an in depth interview with the chair Mr Micin Ali. He also conducted interviews in Dubai and Hargeysa with the owners and senior mangers of twelve MSBs as well as senior staff members of leading Telcos including Telesom, NationLink and the director of Somaliland Association of Telcom Operators. Furthermore, essential discussions were carried out with ZAAD's senior staff, Salaam Bank, and Governor of Somaliland Bank as well as four Somaliland Government Ministers and political leaders, a board member of the Somaliland Electoral Commission and directors of four local NGOs. Giulia Liberatore conducted interviews in 2013 with directors of Somali MSBs, community activists and other stakeholders involved in the Safer Corridor Pilot Project in London. She also interviewed government officials, directors of MSBs and of other financial institutions in Hargeysa, Somaliland. This research was conducted as part of the project entitled 'Diaspora engagement in war torn societies,' funded by the Leverhulme Trust under the Oxford Diasporas Programme.

2. However, in early June all 13 licenses were reinstated by the Central Bank of Kenya after it had carried out due diligence on critical compliance matters concluding that financial regulations were satisfied.

3. Lindley, A and Mosley, J. (2014) Challenges for the Somali Money Transfer Sector. Nairobi, Kenya: Rift Valley Institute Briefing Paper, pages 4–5.

4. Hammond, L. et al (2013) Family Ties: Remittances and Livelihoods Support in Puntland and Somaliland. Food Security and Nutrition Analysis Unit—Somalia. Anecdotal evidence suggests that actual numbers far more exceed 2 billion per year.

5. Watkins, K & Quattri, M (2014) Lost in intermediation: How excessive charges undermine the benefits of remittances for Africa. ODI.

6. World Remit operates online and remains the only organization that is able to escape the account closures. Its model eliminates actual cash transfers while meeting all the necessary international financial regulations. In general financial regulators argue that greater cash flows and circulations undermine important compliance procedures

whereas online money transfers offer more transparency which satisfies regulatory demands.

7. Oxfam (2015) Hanging by a Thread: The Ongoing threat to Somalia's remittance lifeline and Oxfam (2014) Keeping the Lifeline Open: Remittances and Markets in Somalia.

8. Dfid (2015) Safer Corridor Pilot for UK-Somali Remittances: Stakeholder Engagement Summary: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/418688/15-03-20_SCP_Stakeholder_Engagement_Summary.pdf

9. Several other consultancy projects were commissioned throughout the duration of the project. For example, Beechwood International were funded to produce the 'Safer Corridors Rapid Assessment: Somalia and UK' report in 2013.

11. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/348648/Money-laundering-guidance-for-money-service-businesses.pdf

12. For an update on the UK government's involvement in the Safer Corridor Project and Initiative see: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/471064/UK-Somalia_Safer_Corridor_Initiative.pdf

13. In addition, MSBs cater for business customers including (I)NGOs, which normally involves a bank to bank transfer. For further information on how the remittance system works see A. Lindley (2009) 'Between 'dirty money' and 'development capital': Somali money transfer infrastructure under global scrutiny,' African Affairs, 108 (433), and M.H. Hassan and C. Chalmers (2008) UK-Somali Remittances Survey. Dfid

14. MoneyCorp is a UK-based company which offers foreign exchange services to individuals and companies, and Choice is a payment service provider which offers a range of payment options—from bank account transfers, to cash pick-ups and mobile wallet top ups.

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