

Testimony of Douglas Farah

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Before the Task Force to Investigate Terrorism Financing
House Committee on Financial Services

The Next Terrorist Financiers: Stopping Them Before They Start

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Chairman Fitzpatrick, Ranking Member Lynch, and members of the Task Force:

Thank you for the opportunity to testify on the important issue of the changing nature of terrorist financing. I want to state clearly that I speak only for IBI Consultants and myself at this hearing, and not on behalf of either the National Defense University or CSIS.

I have been asked to address new mechanisms that terrorists are using to finance their activities, hide and move the value of their resources, and generate income. I would like to address several issues that I think are important, and that are often carried out in conjunction with transnational criminal organizations (TCOs).

A Historic Overview and the Rise of “Criminalized States”

In my three decades of focusing on transnational crime and 15 years working extensively on threat finance issues, I have found that there is very little new under the sun. Some new domains, such as cyber, have emerged and offer different alternatives but most of the money moves through the same general structures that they have for many years. These include trade based money laundering; the use of commodities such as diamonds, emeralds, and gold; bulk cash shipments; and informal money transfer systems.

The use of gold and precious stones by terrorist groups and TCOs has been widely documented but little understood. In 2002, I wrote a front-page investigation in the *Washington Post* on how al Qaeda and the Taliban used gold for financial transactions and how the organizations shipped millions of dollars in gold from Afghanistan and elsewhere to Dubai immediately following 9/11. It was one of the key financial lifelines that allowed the organizations to survive.¹

In 2004 I wrote a book on how al Qaeda, Hezbollah and other terrorist groups, as well as multiple criminal syndicates used West Africa’s “blood diamond” trade to move and store millions of dollars of value.² My colleague here today, John Casara, was one of the first in the U.S. government to try to focus on gold issues and has written extensively and compellingly on the issue.

Those terrorist organizations used these methodologies for the same reason Colombia’s Revolutionary Armed Forces of Colombia (*Fuerzas Armadas Revolucionarias de Colombia – FARC*), Hezbollah and other terrorist groups use them today – because it is easy, low risk and largely unregulated. Dubai remains the center of the world gold and diamond trade and virtually every major gold bullion firm under investigation or convicted in the use of gold for terrorist financiers has a significant presence in that Emirate.

What has changed in recent years is the volume of the streams of illicit money flows in which terrorists and allied TCOs can hide their money movements. There are many factors at play in the rapid expansion of these flows, but I would like to start by reiterating a

¹ Douglas Farah, “Al Qaeda’s Road Paved with Gold: Secret Shipments Traced Through Lax System in United Arab Emirates,” *The Washington Post*, February 17, 2002, p. A01.

² Douglas Farah, *Blood From Stones: The Secret Financial Network of Terror*, Broadway Books, New York, 2004.

concept or a construct that I shared with this task force when I testified before you in May 2015: criminalized states and the hybrid criminal/terrorist structures they support.

By criminalized state I mean states where the senior leadership is aware of and involved – either actively or through passive acquiescence – on behalf of the state, in transnational criminal organizations (TCOs), where TCOs are used as an instrument of statecraft, and where levers of state power are incorporated into the operational structure of one or more TCOs.³ In these states the government, relying on revenues from illicit activities to survive, often facilitate the overlapping activities with different terrorist organizations.

The existence of these criminalized states in Latin America, Africa, and parts of the former Soviet Union is a primary factor that facilitates terrorist and TCO financial movements, today, and one that has allowed for a significant increase in these activities. The fact that these illicit flows are embedded within state structures is also one of the key factors in making it difficult to halt such financial flows or to punish those engaged in such illicit activities.

This emerging combination of threats comprises a hybrid of criminal-terrorist and state- and non-state franchises, combining multiple nations acting in concert, and traditional TCOs and terrorist groups acting as proxies for the nation-states that sponsor them. No longer is the state/non-state dichotomy viable in tackling these problems, just as the TCO/terrorism divide is increasingly disappearing.⁴

In the Western Hemisphere, it is the involvement of numerous states led by Venezuela in an ongoing criminal enterprise that make disrupting and dismantling the financial networks so difficult. The government of Nicolás Maduro, along with the governments of Evo Morales in Bolivia, Rafael Correa in Ecuador, Daniel Ortega in Nicaragua and Salvador Sánchez Ceren in El Salvador, view the Revolutionary Armed Forces of Colombia (*Fuerzas Armadas Revolucionarias de Colombia – FARC*), a designated terrorist organization by the United States and Europe,⁵ as well as a major cocaine trafficking organization, as a strategic ally.

This same bloc of countries, grouped under the umbrella of the Bolivarian Alliance for the Peoples of Our America (*Alianza Bolivariana Para los Pueblos de Nuestro America – ALBA*), has actively helped Hezbollah, the Spanish separatist ETA organization and other designated terrorist entities to establish a significant presence in Latin America. Hezbollah, in turn is a proxy for the nation of Iran and has access to the financial structures discussed

³ This definition is drawn from my study of transnational organized crime in Latin America. For a full discussion see: Douglas Farah, *Transnational Organized Crime, Terrorism, and Criminalized States in Latin America: An Emerging Tier-One National Security Priority* (Carlisle, PA: Strategic Studies Institute, U.S. Army War College, August 2012), accessed at:

<http://www.strategicstudiesinstitute.army.mil/pubs/display.cfm?pubID=1117>

⁴ Douglas Farah, *Transnational Organized Crime, Terrorism, and Criminalized States in Latin America: An Emerging Tier-One National Security Priority*, op cit.

⁵ “FARC Terrorist Indicted for 2003 Grenade Attack on Americans in Colombia,” Department of Justice Press Release, September 7, 2004. accessed at:

http://www.usdoj.gov/opa/pr/2004/September/04_crm_599.htm and: Official Journal of the European Union, Council Decision of Dec. 21, 2005, accessed at: http://europa.eu.int/eurlex/lex/LexUriServ/site/en/oj/2005/l_340/l_34020051223en00640066.pdf

below because their own state sponsor –Iran – protects them and Iran’s Latin American allies in ALBA.

In my previous testimony, I discussed the vast flows of inexplicable resources that wash through the ALBA government financial structures. Both presidents Ortega in Nicaragua and Sánchez Cerén in El Salvador are former leaders of revolutionary movements in their home countries and have deep historic and abiding ties to both the FARC and the Chávez/Maduro criminal structure.

Ortega has publicly acknowledged receiving some \$500 million dollars a year that flow directly to him and his family members, reportedly from the sale of subsidized Venezuelan oil through the state run company Albanisa. However, little such oil actually exists. Yet the money flowing through the Albanisa structure is equivalent to about 20 percent of the nation’s annual budget, but is completely unregulated and unaccounted for.

In El Salvador, the governing Farabundo Marti National Liberation Front (FMLN) controls ALBA Petr6leos, which is 60 percent owned by PDVSA, the Venezuelan state oil company. Snchez Cern is a member of the ALBA leadership, as is Ortega.

According to public statements of FMLN leaders such as Jos Luis Merino, ALBA Petr6leos began with \$1 million from PDVSA in 2007 and by the end 2013 had revenues of \$862 million, with no explanation for the massive growth.⁶ Merino, who is a senior ALBA Petr6leos advisor, publicly stated that he knew that “many people are nervous because ALBA Petr6leos was born six or seven years ago with \$1 million and now has \$400 million. Let me correct myself, \$800 million, and we are trying to change the lives of Salvadorans.”⁷ The following year ALBA Petr6leos leaders said the company generated \$1 billion in revenues. Yet there is no legal economic activity to undergird anything close to that amount of revenue.

This represents about 23 percent of the national budget. However, like Albanisa, the revenues do not flow into the national treasury, are not allocated through the normal budgetary process and are subject to no oversight. They are directly controlled by party elites, with no accountability. Investigations in El Salvador show that the ALBA Petr6leos structure has moved at least \$291 million through eight shell companies to offshore safety in Panama.⁸

The Growing Importance of Gold in TCO and Terrorist Structures

Within the context of these vast, economically irrational money flows already moving through criminalized states, the growing amount of unusual mining and exporting of minerals, particularly gold in Latin America must be viewed with concern.

The relatively high price of gold, coupled with the ease of movement, ease of placement and sale, and a striking lack of control over the movement of the commodity make it particularly

⁶ These figures are taken from ALBA Petr6leos official financial filings.

⁷ “Jos Luis Merino defiende a Alba Petr6leos por ataques de ANEP,” Verdad Digital, October 31, 2013.

⁸ Efrn Lemus, “Alba tiene ocho offshore en Panam y as reduce impuesto en El Salvador,” El Faro, April 11, 2016, accessed at: http://www.elfaro.net/es/201604/el_salvador/18388/Alba-tiene-ocho-offshore-en-Panam%C3%A1-y-as%C3%AD-reduce-impuestos-en-El-Salvador.htm

attractive to both criminal and terrorist groups. The fact that gold movements are not required to be reported as financial transactions mean that almost-pure ore can be moved with great ease and little risk, and converted to cash almost immediately and again at little risk.

It is even easier if state institutions, rather than trying to find and halt the illicit movements of gold are complicit in that movement across borders. U.S. and European law enforcement investigations have documented multiple cases of Venezuelan government officials, in addition to aiding and abetting the flow of FARC-produced cocaine to the United States and Europe, moving gold illegally through the free trade zones of Curacao, Panama and elsewhere.

As one recent study noted, “There are two broad characteristics of gold and the gold market which make it enticing to criminal groups. The first is the nature and size of the market itself, which is highly reliant on cash as the method of exchange. The second is the anonymity generated from the properties of gold, which make tracking its origins very difficult to do. These factors make gold highly attractive to criminal syndicates wishing to hide, move or invest their illicit proceeds.”⁹

Due to the almost complete lack of risk, moving gold is increasingly becoming a preferred method of payment for other illicit products, such as cocaine. And in some cases, illegal mining is replacing cocaine trafficking as the primary illicit commodity moved to the international market.¹⁰

“Today criminal mining moves more resources to illegal groups, the guerrillas and mafias, than narco-trafficking,” said Colombian President Juan Manuel Santos last year. He estimated the revenue from illegal gold mining to be more than \$2 billion.¹¹

According to one study, while it takes six months to grow coca and process a kilo of cocaine, along with significant technical skills, low-cost and low-skill gold mining in the Colombian jungle can yield 2 kilos a month. In addition, “a kilogram of cocaine can sell for about 5 million pesos (\$2,570) in the Colombian jungle while a kilogram of gold can fetch 19 times that, or similar to global market prices....The precious metal is also relatively easy to legalize while cocaine remains banned. As soon as it’s excavated and away from the mine it’s legal.”¹²

As the inter governmental Financial Action Task Force (FATF) noted in its 2015 report title “Money Laundering/terrorist financing: Risks and vulnerabilities associated with gold,”

⁹ Financial Action Task Force, “Money laundering/terrorist financing: risks and vulnerabilities associated with gold,” July 2015, accessed at: <http://www.fatf-gafi.org/media/fatf/documents/reports/ML-TF-risks-vulnerabilities-associated-with-gold.pdf>

¹⁰ “Minería ilegal desplaza a la coca en ocho regiones,” El Tiempo (Colombia), September 12, 2012, accessed at: <http://www.eltiempo.com/archivo/documento/CMS-12214227>

¹¹ “Minería supera al narcotráfico en ingresos: Santos,” CM& Noticias, August 11, 2015, accessed at: <http://www.cmi.com.co/mineria-supera-al-narcotrafico-en-ingresos-santos>

¹² Cecilia Jamasmie, “Illegal gold profits for rebels in Colombia five times larger than cocaine,” Mining.com, June 24, 2013, accessed at: <http://www.mining.com/illegal-gold-mining-profits-for-rebels-in-colombia-five-times-larger-than-cocaine-68592/>

Gold is an extremely attractive vehicle for laundering money. It provides a mechanism for organised crime groups to convert illicit cash into a stable, anonymous, transformable and easily exchangeable asset to realise or reinvest the profits of their criminal activities.

*The gold market is a target for criminal activity because it is highly lucrative. Understanding the various stages of the gold market continuum, and the types of predicate offending that can occur in each stage, is critical in identifying money laundering and terrorist financing risks emanating from this industry.*¹³

Because of the ease of using gold, where many large gold smelting and refining companies act as banks as well as commodity brokers, when the formal financial system comes under pressure, this is an easy, low risk and cost free alternative.

When the U.S. government's inter-agency investigation successfully took action against the Lebanese Canadian Bank (LCB) in 2011, designating the bank both a "primary money laundering concern" and primary financial vehicle for Hezbollah, the bank collapsed.¹⁴ This left multiple important stakeholders with the need to find alternative financial service providers and ways to both launder and move cash value. Recent U.S. and European law enforcement investigations show that many of those providing financial services to Hezbollah and TCOs through LCB are now moving resources through a web of gold companies based in Dubai.

This new rush to gold has brought noticeable distortions to the gold market, though few steps have been taken to examine them. Those using gold often disguise the origin of the gold so as to avoid scrutiny in the country of origin. Thus Peruvian gold purchasers may move the gold out of Medellín, Colombia, and show the origin as Colombian, a situation that led to a time recently when Colombia on paper was exporting more gold than it actually produced.

Because the FARC and its allies in Venezuela want to disguise the origin of their gold after it is mined, they often move it through Guyana, Suriname, Nicaragua and/or Ecuador to avoid detection of gold entering the market from places where such movements would arouse suspicions of TCO and terrorist connections.

A joint investigation by *Ojo Público*, a consortium of news outlets in South America, into gold mining found that:

*Through a travel to mining centers in Peru, Bolivia, Ecuador and Colombia, accessing to judicial and police documents on illegal trafficking of metal and analyzing the exportation of gold from South America, **OjoPúblico** identified the major financiers of the gold fever that has devastated large parts of South America in recent years—a group of companies from the US, Switzerland, Italy and the United Arab Emirates, associated or linked to the London Bullion Market Association (LBMA), the union that sets the international price of gold and that gathers the major traders of this asset in the world.*

¹³ Financial Action Task Force, op. cit.

¹⁴ U.S. Department of Treasury, "Treasury Identifies Lebanese Canadian Bank Sal as a 'Primary Money Laundering Concern,'" Press release, February 10, 2011, accessed at: <https://www.treasury.gov/press-center/press-releases/Pages/tg1057.aspx>

These companies -Metalor Technologies and MKS Finance, from Switzerland; Northern Texas Refinery (NTR Metals) and Republic Metals Corporation (RMC), from the US; Itaipreziosi from Italy and Kaloti group from the emirate of Dubai-, are also suspected of buying hundreds of tons of illegal gold from south American exporting firms managed by illegal mining operators linked to money laundering, organized crime and cross-border smuggling of metal. The judicial authorities of Peru have targeted these companies (which also acquire gold in Medellin, La Paz and Guayaquil) because of the 25 criminal cases opened after the confiscation of one ton of metal in Callao between 2013 and 2014, and because of other processes of money laundering from illegal mining.”¹⁵

The same consortium later found that many of the companies it had traced in its original investigations had set up an offshore financial structure in the British Virgin Islands (BVI) under the guidance of the Mossak Fonseca law firm based in Panama but with offices operating in Lima, Peru and elsewhere.¹⁶

The case of Goldex, where the company was accused by Colombian officials of laundering billions of dollars for the FARC and other criminal organizations, shows the template of how illicit gold moves and is used for laundering.

Colombian prosecutors handling the case say the company moved some 47 tons of gold, valued at \$1.4 billion, over a six-year period prior to the arrest of its leader. Goldex records showed a host of anomalous and illegal activities that were carried out but are seldom investigated or prosecuted. In this case, however, prosecutor Luz Angela Bahamon concluded that “it is not possible to come to any conclusion except that all of the gold and all of this income they were trying to justify was of illegal origins and came from illegal organizations that needed to create a structure to launder their profits.”¹⁷

The conclusions were based on a series of irregularities that are common in the illicit gold trade and across the world of commodities. As one report noted about the Goldex case:

At the indictment hearing in January this year, the prosecutor described how Goldex sourced its gold from a network of ephemeral supply companies whose life cycle rarely exceeded three years. The companies financed millions of dollars of gold purchases with just thousands in capital and conducted hundreds of transactions in a single day without having a single contract employee, Goldex company records show. Their offices could be found in the most unexpected locations, such as scrapyards or a family home in a village in the state of La Guajira, where the owner swears there has been no gold trading in the 50 years since her great-grandfather built the house.

¹⁵ Óscar Castilla C., Nelly Luna Amancio y Fabiola Torres López, “Dirty Gold: Chasing the Trace of the London Bullion Market,” OjoPúblico, June 9, 2015, accessed at: <http://ojo-publico.com/dirty-gold-chasing-the-trace-of-the-london-bullion-market/>

¹⁶ Óscar Castilla C., “Panama Papers: Las Islas Vírgenes de la Minería Ilegal,” OjoPúblico, April 15, 2016, accessed at: <http://panamapapers.ojo-publico.com/articulo/las-islas-virgenes-de-la-mineral-ilegal/>

¹⁷ James Bargent and Michael Norby, “Blood gold: From conflict zones in Colombia to jewelry stores in the US,” Al Jazeera America, November 18, 2015, accessed at: <http://america.aljazeera.com/articles/2015/11/18/blood-gold-colombia.html>

Purchase records show that the gold these companies supplied to Goldex was bought from thousands of dead people and people who never existed. Yet more of the precious metal was registered as having come from people who told prosecutors they had never been involved in the gold trade, in some cases because they had been living on the streets for years.¹⁸



Figure 1: Illicit Financing/Money Laundering with Gold. Created by Liana Reyes-Reardon, IBI Consultants

The Vital Roll of Offshore Havens

The massive leak of the internal documents of the Panamanian law firm Mossack Fonseca, now known as the Panama Papers, gives an unsettling view of just how easy it is to use law firms in certain jurisdictions to incorporate entities where the real owners are never

¹⁸ Bargent and Norby, op cit.

disclosed, and then use those entities to move massive sums of money to offshore havens where the anonymity is preserved.¹⁹

While privacy issues are real and valid, the current structure represents one of the most glaring weaknesses in the financial structures that are used by a host of illicit actors, including terrorists and TCOs. It is easy but dangerous to forget that al Qaeda and Hamas used extensive offshore structures in the Bahamas to move money around the globe for terrorist groups, including al Qaeda, prior to and following the attacks of 9/11.²⁰

This opaque world overlaps with the vast unregulated world of gold and other commodity movements, and both intersect in the growing number of “criminal state” jurisdictions. This amounts to a perfect storm for terrorist financiers and TCOs to hide and move cash and cash value across the world in ways that are virtually untraceable.

As it stands now, law firms in Panama, Delaware, and multiple other jurisdictions inside and outside the United States can establish a company with bearer shares and that company can then open bank accounts in jurisdictions that pride themselves on bank secrecy. There is no requirement that the real owner(s) of the company or account ever be known.

With those structures in place, large gold refineries acting as banks can then wire the value of gold deposited in their offices to those anonymous companies for deposit in hidden bank accounts.

All of this makes the work of law enforcement difficult if not impossible in tracing financial flows, even when the official strongly suspects the involvement of terrorists TCOs. While this secretive and opaque financial architecture exists, there is very little need for terrorist groups and TCOs to invent a host of new ways to move money and finance their activities. The current system, with its multiple vulnerabilities outside the regulated world where we focus most of our attention, works just fine.

Conclusions

I want to thank the Task Force to Investigate Terrorism Financing for the effort it has put forth to better understand the serious issues associated with this topic, and for the light it

¹⁹ International Consortium of Investigative Journalists, “Giant Leak of Offshore Financial Records Exposes Global Array of Crime and Corruption,” ICIJ, April 3, 2016, accessed at: <https://panamapapers.icij.org/20160403-panama-papers-global-overview.html>

²⁰ In Congressional testimony on February 12, 2002, Assistant Treasury Secretary Juan Zarate the services provided by Bank al Taqwa based in the Bahamas, noting that: “There is some evidence to indicate that those who support terrorist groups use shell banks and companies and perhaps correspondent accounts to collect and move money. On November 7, 2001, the Treasury Department listed Bank al-Taqwa, a Bahamian-based shell bank, as a terrorist financing source. In 1997, it was reported that the \$60 million collected annually for Hamas was moved to accounts with Bank Al Taqwa. As of October 2000, Bank Al Taqwa appeared to be providing a clandestine line of credit to a close associate of bin Laden and as of late September 2001, bin Laden and his al-Qaida organization received financial assistance from the chairman of that bank.” See: Treasury Deputy Assistant Secretary Juan Zarate, “Testimony Before the House Financial Subcommittee,” U.S. Department of Treasury, February 12, 2002, accessed at: <https://www.treasury.gov/press-center/press-releases/Pages/po1009.aspx>

has shed on the financial structures that enable and facilitate the financing of terrorism. While the formal instruments for moving money are understood and regulated, the growing use of commodities and the ease of using anonymous offshore structures remain significant gaps that are easily exploited and seldom examined.

Part of the growing use of gold and other commodities is due to the measureable success the Treasury Department and some of the region's nascent Financial Intelligence Units have had in moving against the formal banking sector. For example, the joint Treasury/DEA case in Honduras late last year against the Rosenthal clan that shut down Banco Continental for its alleged involvement in drug trafficking and money laundering²¹ was an important signal in the region that law enforcement was willing to tackle politically powerful families and their financial institutions.

But little attention is being paid to the multiple anomalies that are blooming across the region. These include: a major diamond polishing center in a region with few diamonds to justify its existence; a gold refinery with capacity to refine four times the annual output of the host country; hosts of gold buying companies with few resources that grow, spread and disappear almost as quickly as mushrooms; small banks operating in marginal jurisdictions that show highly unusual rates of growth in their financial deposits and other activities; and government-sponsored mega projects that claim to spend hundreds of millions of dollars but in reality exist only on paper as a vehicle for laundering money.

Irrational economic behavior on a large scale shrouded in opaque or non-existent reporting is almost always indicative of significant TCO and/or terrorist activities. These behaviors are multiplying, particularly in criminalized states, across the globe. This creates the river that allows the funding of terrorism to grow more difficult to detect and disrupt.

Thank you.

²¹ Steven Dudley, "US Releases Indictment Against Honduran Behemoth," InSight Crime, October 7, 2015, accessed at: <http://www.insightcrime.org/news-analysis/us-releases-indictment-against-honduras-elite>