

Testimony of Douglas Farah

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"Terrorist Responses to Improved U.S. Financial
Defenses"

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Committee On Financial Services

Thank you, Chairman Kelly, for the invitation to talk today about the role of commodities in terrorist financing. I believe it is an extremely important area that has not received the attention it deserves from the intelligence and law enforcement communities, either before or after 9-11.

Commodities such as gold, diamonds and tanzanite have played a vital role in the global terrorist infrastructure. Gemstones have played a particularly important role in al Qaeda's financial architecture. Diamonds, in particular, have been used to raise money, launder funds and store financial value. Gold, for a variety of cultural and logistical reasons, has been used primarily as a way to hold and transfer value. These commodities are not tangential to the terrorist financial structure, but a central part of it.

Diamonds have also been used extensively by Hezbollah and other terrorist groups in the Middle East that have a long tradition of access to diamonds in West Africa through the Lebanese *diaspora* there.¹

Since the late 1990s, diamonds and tanzanite have played an important role in both financing terrorist activities and helping terrorists move their money outside the formal financial sector.² Gemstones are ideal for

several reasons: they hold their value; they are easy to transport; they do not set off metal detectors in airports; and they can be easily converted back to cash when necessary. This is especially true of "blood diamonds," or diamonds mined by armed groups, mostly in sub-Saharan Africa, in order to finance their wars. Diamonds mined in these areas are outside government control, where illicit trade has flourished for year and where it is easy for clandestine structures to operate while drawing little attention from the law enforcement or intelligence communities.

Al Qaeda sought to exploit gemstones in West Africa, East Africa and Europe almost since its inception. Al Qaeda, the Taliban and the Northern Alliance all exploited Afghanistan's emerald fields to finance their activities, so gemstones were not an unknown revenue source.

There is strong evidence of al Qaeda's ties to the African diamond trade, despite the reluctance of some in the U.S intelligence community to acknowledge the link. The data comes from the testimony of al Qaeda members convicted of the 1998 U.S. embassy bombings in East Africa; my own investigations into the ties in West Africa, particularly to Charles Taylor in Liberia and his allies in the Revolutionary United Front (RUF) in Sierra Leone;

investigations by the London-based NGO Global Witness; Belgian police investigations; and most recently, a growing body of evidence accumulated by the U.N.-backed Special Court for Sierra Leone, charged with investigating crimes against humanity in that brutal conflict. In two reports presented to some members of Congress, the Court's chief prosecutor and chief investigator—each with 30 years experience in the Department of Defense—have summarized the large volume of evidence of these ties from sources that are different from and independent of other investigations. I would be happy to provide members of the committee with any of these documents.

Groups like al Qaeda and Hezbollah chose West Africa as a base because in states such as Liberia, Sierra Leone and most others in the region, governments are weak, corrupt and exercise little control over much of the national territory. Some states, like Liberia under Charles Taylor, were in essence functioning criminal enterprises. For the right price, Taylor let al Qaeda, Russian organized crime, Ukrainian organized crime, Balkan organized crime, Israeli diamond dealers and Hezbollah, operate under his protection. Yet Taylor's regime could still issue diplomatic passports, register aircraft, issue visas and enjoy the benefits accorded to a sovereign government.³

Because of this, Taylor issued airplane registrations to Victor Bout, one of the world's largest illegal weapons dealers. Bout was later discovered not only to be selling weapons to most sides of most civil wars in Africa, but also to the Taliban AND the Northern Alliance in Afghanistan. He often took his payment in diamonds. Until very recently he was also flying for the U.S. military in Iraq.⁴

The documentary and anecdotal evidence point to two distinct phases in al Qaeda's diamond activities. The first started sometime before 1996, when bin Laden lived in the Sudan, and was aimed at helping finance the organization. The latter years overlap with the large-scale, al Qaeda dominated purchase of tanzanite in East Africa.

Wadi el Hage, bin Laden's personal secretary until he was arrested in September 1998, spent a great deal of time on gemstone deals. During his trial in New York, El Hage's file of business cards, personal telephone directory and handwritten notebooks were introduced as evidence. He was sentenced to life in prison for his role in the East Africa bombings. The notebooks contain extensive notes on buying diamonds, attempts to sell diamonds, and appraising diamonds and tanzanite. There is a page on Liberia, with telephone numbers and names. His address book and business

card file were full of the names of diamond dealers and jewelers, many containing the purchaser's home phone number.

It is not clear how profitable al Qaeda's gemstone ventures were. What is clear is that the efforts to acquire gemstones, particularly diamonds, were frequent, widespread and a matter of priority of al Qaeda.

In late 1998, following the al Qaeda attacks on the U.S. Embassies in Nairobi, Kenya and Dar-es-Salaam, Tanzania, al Qaeda moved to the second phase of its diamond operation. The impetus was the Clinton administration's successful freezing of some \$240 million in assets belonging to Afghanistan's Taliban government and bin Laden, the rogue regime's guest. The move caught both the Taliban and al Qaeda by surprise because they apparently did not realize the money, mostly held as gold reserves in the United States, could be targeted.⁵

The picture of al Qaeda's activities in West Africa changed dramatically in the latter half of 2000, when senior al Qaeda operatives arrived in Monrovia, Liberia. Having set up a monopoly arrangement for the purchase of diamonds through Taylor with the RUF, al Qaeda buyers went on a spree that lasted several months. But here the intention was not to make money, but rather to buy the

stones as a way of transferring value from other assets. In order to do this, the al Qaeda operatives were paying a premium over the going rate for uncut stones, leaving regular buyers without any merchandise to purchase.

What is particularly interesting during this phase was the collaboration between Sunni and Shi'ite Muslims. While al Qaeda operatives on the ground supervised the trade, the middlemen handling the diamonds were Shi'ite. Further muddying the waters as the collaboration between Islamists in the West African diamond trade, with Israeli diamond merchants. Despite the war in their homelands, both Israeli and Lebanese diamond merchants continue to do business with each other. There are numerous other documented cases of al Qaeda-Hezbollah cooperation, but the tie in the financial field is relatively unexplored.

The pace of the al Qaeda purchases picked up beginning in January 2001 and lasted until just before 9/11. Telephone records from the middlemen handling the purchases shows telephone calls to Afghanistan up to Sept. 10. The available evidence points to al Qaeda purchasing some \$20 million worth of RUF diamonds during the 14 months prior to 9/11.⁶ The evidence suggests a rapid, large-scale value transfer operation that allowed the terrorist group to move

money out of traceable financial structures into untraceable commodities.⁷

In the terrorist financial architecture, the use of gold is different than that of precious stones. Gold seems to be used primarily to store value and facilitate the movement of money across the world's financial markets.

Cultural and regional factors made gold a favorite commodity of both the Taliban and al Qaeda. Much of the money they had was stored in gold. In the waning days of Taliban control of Afghanistan, Sheik Omar and bin Laden sent waves of couriers carrying gold bars and bundles of dollars--the treasury of the country and the terrorist movement--across the porous border of Afghanistan into Pakistan.

From the Afghan-Pakistan border area, the money and gold were consolidated and taken by trusted couriers to the port city of Karachi, Pakistan. There, the Taliban consul general Kaka Zada oversaw the movement of the wealth to the desert sheikdom of Dubai, United Arab Emirates. The transfer to Dubai relied on couriers and the virtually untraceable, informal money transfer system known as *hawala*, a method widely used across the Middle East, North Africa and Asia. Zada also personally acted as a courier at

least once, taking \$600,000 in a diplomatic pouch to Dubai in late November 2001.⁸

Such money movements are not unusual. Pakistani officials estimate that \$2 million to \$3 million a day are hand carried from Karachi to Dubai, a flight of less than an hour. But in the three weeks from the end of November to mid-December there was a large spike in the amount of money traveling that route, reaching \$6 million to \$7 million a day. Once in Dubai much of the wealth of the Taliban and al Qaeda was converted to gold bullion and scattered around the world. Gold, unlike cash, is exempt from almost all reporting requirements that govern currencies, making it much harder to trace.

Demand for gold in India and Pakistan is extremely high for religious, cultural and legal reasons. Gold has significance in ceremonial rites for Hindus, and is widely used for dowries in marriages. But for centuries gold has also been the preferred medium of exchange for businessmen and traders on the Indian subcontinent. Gold is a traditional hedge against inflation, hoarded as a security against times of high inflation or hardship. The annual demand for gold in India is estimated by Interpol, the international police agency, to be an astonishing 800 metric tons, almost triple that of the United States.⁹

Because gold imports into both Pakistan and India have traditionally been restricted and subject to high tariffs, gold smuggling from Dubai, where the gold trade is unregulated, has been enormously profitable for decades. Dubai's location is ideal, making it a nexus of myriad smuggling networks that flow through Iran, India, Pakistan, the Arab world, to Afghanistan and Central Asia.

During the war to control Afghanistan, the Taliban was broadly backed by Pakistani and Indian businessmen who wanted a single authority to guarantee their merchandise could move by truck across Afghanistan. The Taliban promised to clear the roadblocks of petty warlords, and in exchange received from the transportation syndicates substantial financial backing, much of it in gold.

Donations to the Taliban and al Qaeda from wealthy Saudi backers were also often made in gold.¹⁰ When U.S.-led forces occupied Afghanistan they found al Qaeda training manuals that included not only chapters on how to build explosives and clean weapons, but sections on how to smuggle gold either on small boats or concealed on the body. Using specially-made vests, gold smugglers can carry up 80 pounds, worth up to \$500,000, on their person. Cash is far bulkier.¹¹

Gold continued to play a vital role in al Qaeda finances in recent times. In the summer of 2002, elite European intelligence units monitoring al Qaeda's movements forwarded an alarming report to their U.S. counterparts: Al Qaeda and the Taliban were shipping large quantities of gold through Karachi to Sudan. The gold was being sent by boat to either Iran or Dubai, where it was mixed with other goods and flown by charter airplanes to remote airstrips in Sudan. The gold was obtained through a "commodity-for-commodity exchange," Pakistani intelligence officials said, meaning heroin and opium stashed by the Taliban and al Qaeda was traded to drug traffickers for the precious metal. The gold was packed in boxes and represented only a small portion of the cargo on each charter flight. Estimates of the value of the gold ranged from several hundred thousand dollars to several million.¹²

Sudan was familiar territory for bin Laden, and his history there has been retold often. But it is worth a brief recap.

In April 1991, he had moved there with several hundred combatants, welcomed by the fundamentalist Islamic government, the National Islamic Front. Bin Laden even married into the family of NIF leader Hassan al Turabi, wedding Turabi's niece.¹³

In May 1996, under heavy pressure from the United States and anxious to rehabilitate its international image, Sudan asked bin Laden to leave, and he returned to Afghanistan. However, many of bin Laden's businesses in Sudan remained active and he remained close, economically and politically, to many leaders of the NIF. Bin Laden "has banking contacts there, he has business contacts there and he is intimately familiar with the political and intelligence structure there," said a European intelligence official. "He never fully left Sudan despite moving to Afghanistan."¹⁴

There are several lessons one can draw about the financing of Middle Eastern terror in West Africa and the terrorist use of commodities.

One is that terrorist groups are sophisticated in their exploitation of "gray areas" where states are weak, corruption is rampant and the rule of law nonexistent. They correctly bet that Western intelligence services do not have the capacity, resources or interest to track their activities there.

A second lesson is that terrorist groups in these areas learn from their own mistakes as well as each other. They are adaptable in ways that make them extremely hard to

combat. Hezbollah has been using diamonds from West Africa to finance its activities for at least 20 years, perfecting smuggling routes to Europe and Lebanon, developing a network of middle-men and successfully embedding its financial structure within the diamond trade. Al Qaeda operatives plugged into the same network.

A third lesson is that small clues and critical analysis matter in tracing terrorist funding and the use of commodities, but there has been a limited understanding of the financial structure of al Qaeda and Hezbollah before and after 9/11. The intelligence community carried out its first comprehensive assessment of al Qaeda's financial structure in 1999. The 9/11 Commission found the same to be true for the entire intelligence community in looking at al Qaeda's organizational structure. Rather than understanding the complex web of commodities, charities and individual donors that filled al Qaeda's coffers, the conventional wisdom in the intelligence community was that bin Laden was using his personal wealth to finance his organization's operations.

A fourth lesson is that terrorist networks and criminal networks can overlap and function in the environments of failed states, like that of Liberia. Commodities like diamonds are the coin of choice as the

different groups provide different services to governments or rebel groups in exchange for cheap access to commodities.

A fifth lesson is that the intelligence community reacts very poorly to information it does not initiate. Within the culture of the community, the assumption was that the initial diamond stories made the CIA look bad, and therefore had to be attacked. So was the information passed on by Special Court for Sierra Leone investigators. More than two years later the tide is changing. But if the terrorist use of commodities is to be understood and effectively cut off, the intelligence community must begin to look beyond the traditional methods of raising and moving money, and begin to look at commodities more seriously.

There are several steps that must be taken to begin to combat the use of commodities by terrorists.

The weapon most often brandished, but that is the least effective, is to institute new, sweeping regulations on commodity traders. This will simply drive even legitimate businessmen underground or out of business. New regulatory burdens to halt the fraction of illegal activities that benefit terrorists in the diamond industry, gold trade or *hawala* transactions would hurt millions of

people. This is especially true of the *hawala* system, which primarily benefits millions of families in India and Pakistan who live off the remittances sent through this system by family members working on the Arab Peninsula.

What is really needed is the most difficult and time consuming to carry out: building up intelligence-gathering capabilities on the ground in the "grey areas" or "stateless areas" of the world where the illicit commodity trades flourish and where terrorists have made significant inroads. These areas include parts of West Africa, much of the Democratic Republic of the Congo, parts of East Africa and swaths of Southeast Asia. Only specific information gathered at the points of origin in the commodities trade can really help monitor and decipher how the businesses operate.

For example, in Sierra Leone, Liberia and the DRC, a network of Lebanese diamond traders, related by family and political ties, have traditionally moved the bulk of the "blood diamonds." These kinship networks that are central to this commodity trade need to be mapped and understood as a first step toward defining what action can be taken. It is also essential to understand these groups, operating in areas of the world where computers and telephone communication is haphazard at best, rely on personal

contacts, family ties and couriers for much of their operating structure. High-tech monitoring of their communications, successful against other types of groups, is much less useful in these circumstances.

The intelligence deficiencies are not surprising. At the end of the Cold War, no region of the world suffered more dramatic intelligence cuts than sub-Saharan Africa. More than one-third of the CIA stations were eliminated entirely and those that remained were left with only minimal staffing. Even as the Clinton administration began increasing funding for intelligence in the late 1990s, the region's capabilities and budget remained static.¹⁵

As the capacity to monitor events on the ground is being rebuilt, there are steps that can have an impact. The most urgent is to begin to seriously work with the commodity industries themselves. There is a knowledge base there that can be tapped into, because many of the important players are not only concerned about terrorists' use of their commodity. They also want to clean up their image. While unwilling to act as government agents, many in these communities are willing to share information and ideas on how to clean up and safeguard particular trades. This is important because these groups are small and know

the players. Many are anxious to help put the more disreputable elements out of business.

Nicky Oppenheimer, chairman of the De Beers Group and an important voice in the diamond community, has recognized that the terrorist threat is real. In March 2004 he said that among the greatest challenges facing the diamond and jewelry industry "is the vulnerability of the industry, as with other commodities, to misuse and abuse by criminals and the perpetrators of terror...In a world where our personal security, that of our families and communities, is under real and present threat, we must take notice and take action."¹⁶

Efforts to deprive terrorists of their funds means, necessarily, depriving them of their safe havens. The new havens are in parts of the world we have long ignored, the spreading swaths of stateless territories and rogue regimes. Until we recognize this and begin to understand the true nature of terrorist finance, their money will continue to flow.

Given the nature of the transactions, the growing pace of globalization and the untraceable nature of these transactions, they are likely to remain an integral part of terrorist financial structure for the foreseeable future.

¹ For a fuller discussion of the Lebanese role, including that of Hezbollah and the Amal militia, please see Lansana Gberie, *War and Peace in Sierra Leone: Diamonds, Corruption and the Lebanese Connection*, The Diamond and Human Security Project, Occasional Paper 6, January 2003. Also, Harris, Edward, "Hezbollah Extorting Funds From West Africa's Diamond Merchants," *The Associated Press*, June 29, 2004.

² For a fuller discussion of al Qaeda's ties to the tanzanite trade, see Robert Block and Daniel Pearl, "Underground Trade: Much Smuggled Gem Called tanzanite Helps bin Laden Supporters," *Wall Street Journal*, Nov. 16, 2001, p. A1. For a description of al Qaeda's ties to the diamond trade, see Douglas Farah, "Report Says Africans Harbored al Qaeda," *Washington Post*, Dec. 30, 2002, p. A1; also Global Witness, *For a Few Dollars More: How al Qaeda Moved into the Diamond Trade*, London, 2003.

³ Farah, *Blood From Stones*, op cit.

⁴ Braun, Stephen, Judy Pasternak and T. Christian Miller, "Blacklisted Russian Tied to Iraq Deals; The Alleged Arms Broker is Behind Four Air Cargo Firms used by U.S. Contractors, Officials Say," *The Los Angeles Times*, Dec. 14, 2004, p. A1.

⁵ Daniel Benjamin and Steven Simon, *The Age of Sacred Terror*, Random House, New York, 2002, p. 289.

⁶ Belgian police report, "Case LIBI," obtained by author.

⁷ Farah, *Blood From Stones*," op cit.

⁸ This information was obtained through interviews with knowledgeable sources in Pakistan and Dubai, and first reported by me in the *Washington Post* Feb. 17, 2002, pg. A1, "Al Qaeda's Road Paved With Gold."

⁹ Interpol Report, *Gold Smuggling and the Drug Trade in Southwest Asia*, obtained by author

¹⁰ Confidential author interviews

¹¹ Farah, *Washington Post*, op cit

¹² Douglas Farah, "Al Qaeda Gold Moved to Sudan," *Washington Post*, Sept. 3, 2002, page A1.

¹³ Prof. Eric Reeves, leading Sudan expert, Smith College, North Hampton, MA., e-mail communication, Feb. 20, 2003

¹⁴ Farah, *Sudan*, op cit

¹⁵ Author interviews with intelligence officials. Also, Farah, Douglas, *Blood From Stones: The Secret Financial Network of Terror*, Broadway Books, New York, 2004.

¹⁶ Address of Nicky Oppenheimer, chairman, De Beers Group, to the World Diamond Council Third Annual Meeting, Dubai, March 30, 2004.