



GLOBAL FINANCIAL INTEGRITY

**House Financial Services Committee
Subcommittee on National Security, International Development, and
Monetary Policy**

**Hearing on
Schemes and Subversion: How Bad Actors and Foreign
Governments Undermine and Evade Sanctions Regimes**

**Statement of Lakshmi Kumar
Policy Director**

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Chairwoman Waters, Ranking Member McHenry, distinguished members of the Subcommittee on National Security, International Development, and Monetary Policy, it is an honor and privilege to testify before you today on the critical subject of the schemes utilized by criminal actors and bad governments to evade and undermine the U.S. sanctions regime. I am immensely grateful for the invitation and the opportunity to join this esteemed panel.

The U.S. with over 30 sanctions programs¹ has an expansive sanctions regime that is utilized to target “*individuals, corporate entities (e.g., firms, political parties, or other nonstate actors such as UNITA, al-Qaeda, ISIL), sectors of an economy (e.g., aviation or arms, financial, or commodities such as oil, diamonds, or timber); or specific regions of a country (as in Darfur in western Sudan).*”² Recent advisories including the May 2020, the U.S. Departments of State, the Treasury, and the U.S. Coast Guard Advisory - “Sanctions Advisory for the Maritime Industry, Energy and Metals Sectors, and Related Communities”³ have sought to emphatically place the compliance burden outside their purview of large financial institutions and corporations. This is also reflected in the most enforcement actions by OFAC that target industries beyond the domain of financial services. “*Of the 25 enforcement actions OFAC pursued in 2019-2020, only four involve financial institutions.*”⁴

However, successful compliance of U.S. sanctions measures is predicated around an in-depth understanding of complex legal structures, sectoral understanding (how oil, gold, or timber trading works), and financial and trade arrangements. Yet actors seeking to evade and undermine U.S. sanctions exploit vulnerabilities in U.S sectors and industries that are ill-equipped to mitigate against the threats of illicit financial flows, corruption, and money laundering. Furthermore, because sanctions evasion techniques exist in a world where financial and trade networks are globally inter-connected, evasion occurs as a result of the cracks not just in the U.S. regulatory architecture but also due to weaknesses in the statutory and regulatory framework of other countries. These include safe havens and secrecy jurisdictions⁵, jurisdictions that have weak rule of law or systemic corruption⁶, jurisdictions with nascent policies to target illicit finance that struggle with both technical and technological capacity, and, finally, the global networks of professionals that help channel money, create legal

¹ [US Sanctions Programs](#)

² U.S. Senate Committee on Foreign Relations, [U.S. SANCTIONS POLICY IN SUB-SAHARAN AFRICA](#), (June 8, 2016)

³ [Sanctions Advisory for the Maritime Industry, Energy and Metals Sectors, and Related Communities](#)

⁴ [Navigating the Sanctions Minefield: What Every Global Business Should Know](#) (June 5, 2020)

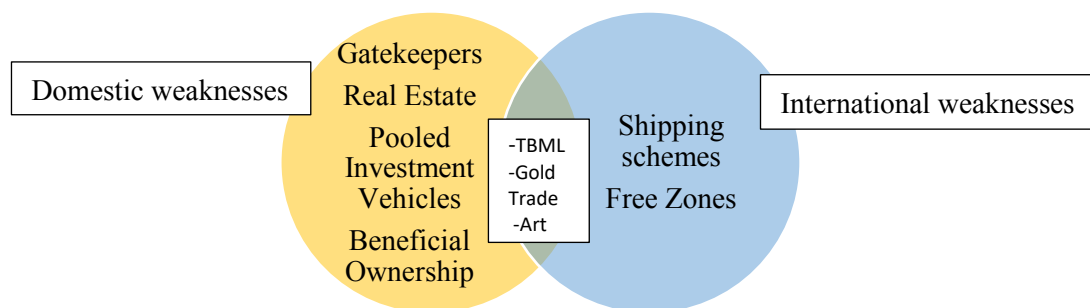
⁵ Jodi Vittori and Matthew T. Page, [Dubai’s Role in Facilitating Corruption and Global Illicit Financial Flows](#), (July 07 2020)

⁶ [How 7.4 Tons of Venezuela’s Gold Landed in Africa—and Vanished](#), WSJ (June 18, 2019)

structures to obscure identity, find creative ways to hide money, all for a sizeable monetary compensation that is often re-routed back into the U.S. economy⁷.

What lends further difficulty in detecting sanctions evasion schemes is the complexity of ‘how’ and ‘who’ U.S. sanctions programs target. The ‘who’ reflects not only the complexity of schemes utilized to evade and undermine U.S. sanctions but also reveals the type of resources that are available to be deployed to evade sanctions.⁸ Sanctions that target a critical sector of an economy⁹, or, an individual with a close relationship to the ruling elite,¹⁰ are harder to enforce because there are few checks in the home jurisdiction where the entire resources of the State and government are dedicated to evading sanctions (the ports, financial institutions, law enforcement etc.).¹¹ Conversely, schemes by individuals/corporate entities/ non-state organizations to evade sanctions depending on context do not automatically benefit from the vast resources of the state and rely on weak or willing governments, complicit individuals and the difficulty of enforcement and absence of adequate oversight and regulation especially in the arena of trade.

For the purposes of my testimony, I will discuss sectors and industries both in the U.S. and internationally where weak regulatory environments facilitate sanctions evasion.



Use of anonymous companies and complex legal structures: The passage of the Corporate Transparency Act (CTA) represented a monumental stride towards strengthening the ability of the U.S. financial system to combat illicit financial flows. The use of anonymous companies and complex corporate structures that purposefully seek to mask ownership across lengthy horizontal (across multiple jurisdictions) and vertical (several layers of ownership) chains is a consistent feature of all schemes utilized to evade sanctions.¹² This presence in nearly every

⁷ Lakshmi Kumar and Kaisa de Bel, Acres of Money Laundering: Why U.S. Real Estate is a Kleptocrats Dream, July 2021 (forthcoming)

⁸ Iranian oil or Venezuelan oil and gold sectors

⁹ [15 current, former Venezuelan officials charged with narco-terrorism, corruption, drug trafficking and other criminal charges](#) (March 27, 2020)

¹⁰ [Tracing Sanctions Evasion Through Dubai’s Luxury Real Estate Market](#), C4ADS (2018)

¹¹ Ibid

¹² [FACT Sheet: Anonymous Companies and National Security](#), FACT Coalition (January 2020)

sanctions’ evasion scheme underscores the need for FinCEN (as mandated in the CTA) to create a strong and robust registry that can meet the national security needs of the United States.

Trade related schemes: It is important to note that trade related sanctions evasion schemes are separate from trade-based money laundering (TBML) sanctions evasion schemes where value is transferred through the trade transaction itself. In a trade related scheme other trade related offences are used to evade sanctions - (e.g., Where materials related to dual use technologies are traded between companies where the ownership is disguised to evade sanctions). This is simply a trade-related scheme that utilizes anonymous or complex ownership structures, but this does not qualify as a TBML sanctions evasion scheme.

Table A. Trade related Schemes

S.No	Country	Trade related scheme
1	Russia: Export of illegal power turbines	After Russia’s annexation of Crimea, the U.S. imposed sanctions against Russia barring the provision of goods to support Russian deep-water Arctic offshore oil projects. A Russian government-controlled business that wanted to purchase a power turbine from a U.S. manufacturer utilized Russia-, Italy- and U.S.-based companies to evade the sanctions and acquire it for US\$17.3 million. The true end user of the turbine was concealed from both the U.S. manufacturer and the U.S. government by submitting false documentation that stated it would be used by a U.S. company in Atlanta.

Trade Based Money Laundering: Trade based money laundering (TBML) is both a method through which to launder the proceeds of sanctions evasion but also a vital mechanism through which sanctions evasion itself takes place. According to the Financial Action Task Force (FATF), TBML is “*the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illegal origin or finance their activities*”.¹³ Common techniques to disguise the proceeds of crime and move value through trade include misrepresenting the price, quantity, quality, type, volume, and origins of goods. This can be done through over or under invoicing, double invoicing, phantom shipments (where no good is actually moved) etc. The aim of TBML “*is not the movement of goods, but the movement of money, which the trade transactions facilitate.*”¹⁴ Another important distinction is the use of professional money launderers for TBML schemes. Professional money launderers are utilized to “*take receipt of the criminal proceeds (...) and transfer or convert those*

¹³ [Trade Based Money Laundering: Trends and Developments](#), FATF (December 2020)

¹⁴ Ibid

*proceeds, including via TBML schemes, before passing them back (...), minus the payment of their fee or commission”.*¹⁵

Because so many U.S. sanctions target particular commodities like oil, gold, minerals, charcoal, precursor chemicals, dual use technologies, there is a plethora of evidence on the use of TBML schemes to evade sanctions. Sanctions’ evasion schemes tied to TBML are often meant to disguise the origins of the commodity that is being traded or the nature of the commodity itself. Unsurprisingly, the largest ever sanctions evasion scheme is a TBML scheme that allowed Iran to pocket US\$100 billion and exploited both the vulnerabilities in TBML techniques but also the anonymity of the gold trade.¹⁶

Table B - Examples of TBML Sanctions Evasion Schemes

S.No	Country	TBML mechanism
1	Syria: Illegal export of laboratory equipment from the U.S. through third countries ¹⁷	U.K. citizen Ahmed Feras Diri conspired with his brother Harold Rinko, a U.S. resident who owned an exporting firm Global Parts Supply, to ship chemical-warfare measuring equipment and other goods from the U.S. to Syria through Jordan, the U.A.E. and the U.K., without the required license. According to the indictment, <u>they prepared false invoices that undervalued and mislabelled the goods and listed false information regarding the buyer’s identity and geographic location.</u>
2	Venezuela: PDVSA / oil-for-food program evasion scheme	Under the oil-for-food program (exempted from US sanctions), Mexican companies Libre Adorbo and its subsidiary Schlager Business Group were used to help in the resale of Venezuelan crude oil to Asian buyers. Mexican companies claimed to have water and corn delivery contracts with the government, but oil was exchanged for food at inflated prices and food was never delivered (\$300 million program that did not match amount of PDVSA oil deliveries)
3	Iran: Billion-dollar fictitious marble businesses to evade Iranian Oil sanctions	-Kenneth Zong, a professional money launderer entered into fictitious contracts with Iranian controlled companies in Iran and U.A.E. to purchase marble titles from a Dubai-based tile importer and then ship them to an Iranian firm. He never fulfilled this role but instead submitted false contracts, invoices, bills of lading and product documentation to Korean authorities. -Zong opened a bank account with Industrial Bank of Korea (IBK) for his Korean firm, through which he was paid by an Iranian company for the fictitious services provided. Fake invoices were used to convince IBK to release the money. -Zong converted the funds to USD and Euro, before sending wire transfers across the world to companies ultimately controlled by Iranian conspirers in service of the Iranian government. Nearly all of the funds flowed into the UAE.

Trade in Gold and other Minerals: The use and abuse of the gold trade has in the last couple of years received increased attention as a way to generate illicit finance, launder money but

¹⁵ Id

¹⁶ Jonathan Schanzer, [The Biggest Sanctions Evasions Scam in Recent History](#), The Atlantic (January 4, 2018)

¹⁷ [U.K. Man Arraigned on Conspiracy to Illegally Export Restricted Chemical Laboratory Equipment to Syria](#), DOJ (November 13, 2015)

also to evade sanctions. The gold trade in particular is vulnerable to TBML sanctions evasion schemes because gold is easy to transport, transactions are often in cash with no paper trail, gold retains value and most importantly gold preserves anonymity. Much of the attention around the use of gold to evade sanctions has focused on schemes to mask the illicit origins of gold.¹⁸ This is included in international sanctions efforts to limit support for illegal armed groups in the DRC that engage in the illicit trade of natural resources including gold¹⁹ and more recently sanctions targeted on schemes that seek to hide the origins of Venezuelan gold.

In schemes designed to hide the origins of gold, the gold is often exported from a neighboring country where its certificate of origins is falsified. Once the gold is refined, it enters the larger financial systems where its problematic origins and history are erased.²⁰ Using gold to evade sanctions has significantly increased during the pandemic. Record prices of gold, coupled with the ease of anonymity that gold provides make it a perfect vehicle to garner valuable capital for sanctioned entities. Indeed, U.S. imports of gold increased from \$2.68 billion to \$19.96 billion between 2019 to May 2020. This represented a 643.98% increase compared to the previous year.²¹ At the same time, an examination of the movement of Venezuelan gold from news reports shows that to get around U.S. sanctions, Venezuelan gold has flown all over the world and quickly integrated into the international gold supply chain.²² Other drug trafficking groups subject to U.S. sanctions, such as the FARC have utilized the gold trade to continue their operations.²³ The ease with which illicit gold enters the legitimate market makes it nearly impossible to tell if the U.S. is importing the very gold it is trying to sanction.

¹⁸ Lakshmi Kumar, [Illicit Gold Trade: Using Trade Data and Financial Tools to Fight Money Laundering and Transnational Crime](#), ACFC (July 2020)

¹⁹ **Ibid**; [UN report links Uganda to smuggled DRC gold, says exports are underdeclared](#), Uganda Business News (June 20, 2019)

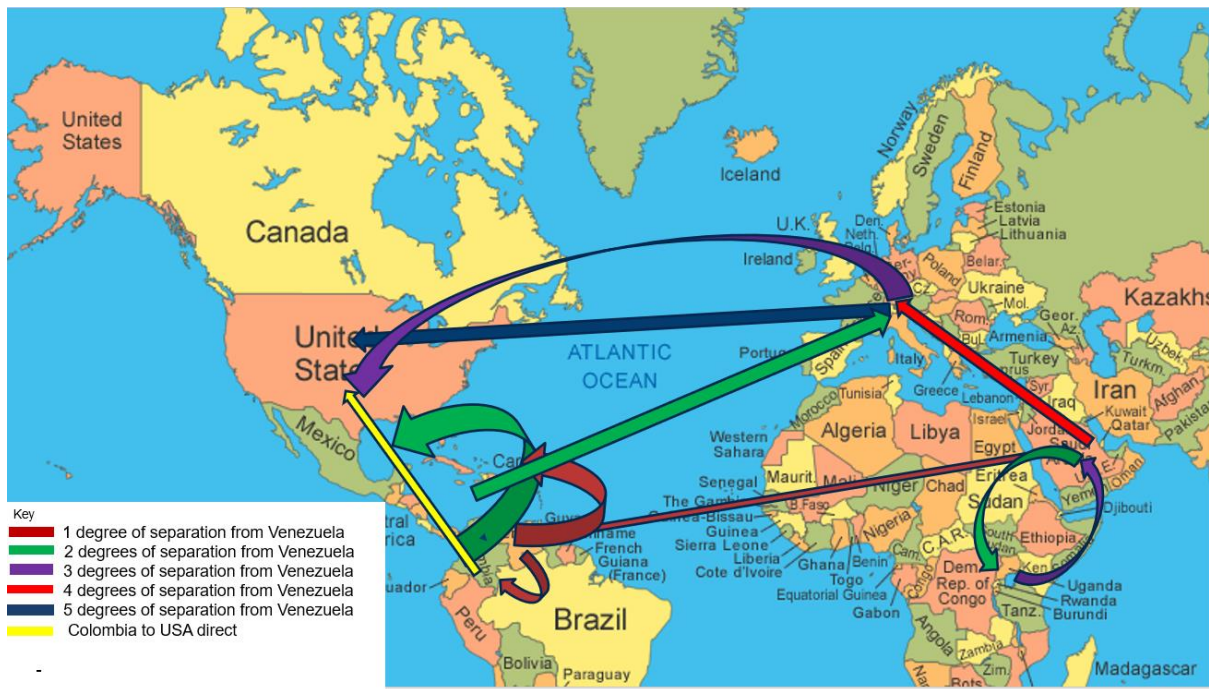
²⁰ Like in the case of the DRC, where the gold is believed to move into Uganda and then gets exported as Ugandan gold.

²¹ Lakshmi Kumar, [Illicit Gold Trade: Using Trade Data and Financial Tools to Fight Money Laundering and Transnational Crime](#), ACFC (July 2020)

²² **Ibid**; [Smugglers Paradise: How Venezuela is using Blood Gold to Circumvent U.S. Sanctions](#)

²³ [The Gold Standard: Addressing IFFs in the Colombian Gold Sector through Transparency](#), Global Financial Integrity (February 2021)

Image A -The complexities of tracking Venezuelan gold²⁴



Finally, the use of gold to evade sanctions is not only restricted to masking the illicit origins of gold, but as seen in the Halkbank sanctions evasion case with Iran, gold can be a critical vehicle in the layering and integration of Iranian oil proceeds into the global financial system to gain access to the U.S. dollar.²⁵

Free Zones: TBML schemes are exacerbated by certain conditions and environments. Free zones provide an environment ripe for trade facilitation but that are also equally convenient for a variety of criminal behavior including sanctions evasion.

Free zones otherwise referred to as free ports, free trade zones, special economic zones and by numerous other names refers to special economic areas that benefit from tax and duties exemptions²⁶ and can be a way to attract business investment into a country. To attract investment into a country, free zones permit businesses to jump through regulatory hurdles quicker. These same benefits that attract legitimate businesses are equally attractive to criminal actors looking to avoid scrutiny when evading sanctions. Factors that increase the risk or likelihood of TBML include less restrictive customs environments, large amounts of paperwork, lack of data, and ports with limited regulation.²⁷ Free trade zones, in particular,

²⁴ Lakshmi Kumar, [Illicit Gold Trade: Using Trade Data and Financial Tools to Fight Money Laundering and Transnational Crime](#), ACFCs (July 2020)

²⁵ Lakshmi Kumar, [Illicit Gold Trade and Using Trade Data and Financial Tools](#), Fintelekt (October 2020); Jonathan Schanzer, [The Biggest Sanctions Evasions Scam in Recent History](#), The Atlantic (January 4, 2018)

²⁶ Daniel Neale, [Free Trade Zones: A Pandora's Box for Illicit Money](#), Global Financial Integrity (October 07, 2019)

²⁷ Lakshmi Kumar, [Chapter 4: Dubai Free Trade or Free For All?](#), Carnegie Endowment (July 2020)

pose a high risk for TBML because because the zones serve as pass through points for goods, i.e transshipment points as opposed to ports of export and import, where there is little customs presence, and little in the way of SAR reporting from free zones. Oversight and accountability is often weak in these zones.

Additionally, free zones are often preferred destinations for schemes involving proliferation financing and dual use goods.²⁸ This is not to say that other sectors like the gold trade that are vulnerable to sanctions evasion and TBML do not use free zones. When gold moves through a free zone, as is often the case with Venezuelan gold that moves through the ABC islands or Dubai, it benefits from the additional layer of opacity that free zones provide, making the substitutions of the origins of gold an easier process.²⁹ Similarly, the Colon free zone in Panama is notorious as a “Mecca” for drug traffickers.³⁰

“To those seeking to evade sanctions, free zones offer something else—a firewall of sorts in the paper trail linking transactions to sanctionable entities or merchandise. Though merchandise may station inside a free zone only for the few hours required to change its accompanying papers, when it departs, its place of origin is the zone itself. By allowing the repurposing of the origin of goods heading from Iran to the West and vice versa, a free zone can unwittingly help obfuscate the real entities engaged in a transaction.... When it can be found, relaxed oversight, insufficient transparency, money laundering, and illicit traffic are the ideal environment for Iranian sanctions evasion.”³¹

Table C: Examples of free zones being utilized in sanctions evasion tied to Proliferation Financing and Dual Use Technologies

S. No	Examples	Nature of use	Location of Free Zone
1	German uranium enrichment components shipped illegally to Pakistan ³²	Transshipment	UAE
2	Mustard gas and nerve agent precursors shipped from India to Iran ³³		
3	Attempted export of a high-speed oscilloscope from the Netherlands to Pakistan ³⁴		
4	Export of maraging steel from Belgium to Iraq ³⁵		
5	U.S. State Department reported that TBML schemes – facilitated by the extensive number of FTZs in the UAE "might support sanctions-evasion networks and terrorist groups in Afghanistan, Pakistan, Iran, Iraq, Syria, Yemen, and Somalia, ³⁶		

²⁸ Refer to Table C

²⁹ Julia Yansura and Lakshmi Kumar, [Narcotics Proceeds in the Western Hemisphere](#), Global Financial Integrity, September 2020

³⁰ Ibid

³¹ Emanuelle Ottolenghi, [“Snap-Back: A Journey Through Iranian Sanctions Evasion in Georgia,”](#) Tablet, July 1, 2015,

³² Ibid

³³ Id

³⁴ Id

³⁵ Id

³⁶ U.S. Department of State, [2016 International Narcotics Control Strategy Report](#) (INCSR), p. 220,

6	Export of heavy water from Germany to India ³⁷		
7	In the case of the H.Q. Khan network, FTZs in Dubai were critical in allowing nuclear technology to reach Iran, DPRK, Libya, and other states ³⁸		
8	In July 2020, the US Department of the Treasury published a settlement agreement with Essentra FZE, a Jebel Ali Free Zone incorporated company, which traded with and accepted payment from North Korea for the illegal export of cigarette filters using deliberately deceptive practices ³⁹		
9	Controlled vacuum pumps exported to Iran via a UAE-based FTZ were given a fake final destination and re-labeled and undervalued as 'spare parts' ⁴⁰		
10	Illegal export of hundreds of controlled pressure transducers from China to Iran ⁴¹	Falsification of documentation to hide cargo	Shanghai
11	An FTZ in North-Korea, the Rason Special Economic Zone, enables Russia and China to get away with sanctions evasion due to a loophole in the sanctions that allows for the entry of goods into North Korea that are ostensibly only transiting through the country and are re-exported to third country destinations ⁴²	Transshipment on paper as a sanction evasion technique	North Korea
12	The Poti Free Industrial Zone (FIZ), located near to the Black Sea port city of Poti, the largest seaport in Georgia, has been used by companies seeking to evade sanctions on Iran ⁴³	Transshipment	Georgia

Shipping Schemes: Accounting for up to 90% of international trade, the maritime industry is also a key artery for sanction evasion. Oil exports by Iran and Venezuela and oil imports by North Korea keep increasing every year despite U.S. sanctions.⁴⁴ Moreover, the number of sanctioned vessels and ports grows with an annual rate of 6%, indicating that the use of ships in sanction evasion is becoming more prevalent.⁴⁵ At the same time, deceptive shipping methods used by bad actors are evolving and becoming more sophisticated with the aim of avoiding detection. Bad actors and rogue states involved in maritime sanction evasion often use a combination of tools aimed at concealment of the cargo, ownership or vessel location.

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³⁸ Ibid at Viksi

³⁹ Federal Register, 'Notice of OFAC Sanctions Actions', 24 August 2020, <https://www.federalregister.gov/documents/2020/08/24/2020-18527/notice-of-ofac-sanctions-actions>

⁴⁰ US Department of Justice, 'Summary of Major U.S. Export Enforcement, Economic Espionage, Trade Secret and Embargo-Related Criminal Cases', June 2016, p.85, https://www.justice.gov/nsd/files/export_case_list_june_2016_2.pdf/download

⁴¹ Viski, A. and Q. Michel (2016), "Viski, A. and Q. Michel (2016), Free Zones and Strategic Trade Controls", Strategic Trade Review, Vol. 2/3, pp. 27-41. https://strategictraderesearch.org/wp-content/uploads/2017/11/STR_03.pdf

⁴² Eric Talmadge, "North Korea beating the odds despite facing toughest sanctions in decades - how?" *The Independent* (London), September 13, 2016,

<https://www.independent.co.uk/news/business/news/north-korea-nuclear-sanctions-china-russia-economic-trade-zone-beating-odds-a7239866.html>

⁴³ Emanuelle Ottolanghi, "Snap-Back: A Journey Through Iranian Sanctions Evasion in Georgia," *Tablet*, July 1, 2015, <https://www.tabletmag.com/sections/israel-middle-east/articles/iranian-sanctions-evasion>

⁴⁴ <https://apnews.com/article/europe-technology-business-1cd3714c9ce906b8fc931ebb95cb9e26>

<https://static1.squarespace.com/static/566ef8b4d8af107232d5358a/t/60585d4086d5b30f0a7f1a5f/1616403804571/BLACK+GOLD.pdf> ; <https://www.mei.edu/publications/iranian-sanctions-evasion-and-gulfs-complex-oil-trade> ; <https://oilprice.com/Energy/Energy-General/Venezuela-Sees-Oil-Exports-Rise-Despite-US-Sanctions.html>

⁴⁵ https://www.regulationasia.com/wp-content/downloads/RA-DowJones_Addressing_Sanctions_Risk_Maritime_Trade.pdf

Use of false flags and flag hopping: To conceal the identity or affiliation of a vessel with a sanctioned state, vessels often falsely represent the flag state that it is registered under or repeatedly change the flag state to avoid detection by authorities (i.e. flag hopping). Even after a vessel gets de-flagged, they continue to claim that flag without the consent or knowledge of that state. In those cases, bad actors often take advantage of poorly run vessel registries or states that do not have the resources to conduct proper due diligence on the vessels in their registries. There are ample reports of North Korea registering under a flag of convenience, i.e. the flag of a country other than the country of ownership, including vessels flagged in Dominica, Hong Kong, China, Panama and Sierra Leone.⁴⁶

Obscuring ownership through complex corporate structures: Bad actors often set up complex corporate structures or frequently transfer ownership of a vessel in order to conceal the beneficial owner ultimately owning the vessel and benefitting from the shipment. To conceal beneficial ownership, bad actors are likely to use companies in jurisdiction without or with weak beneficial ownership registries. In a recent example, of these so-called “shadow ships,” the U.A.E. was exposed as a hub for companies transporting Venezuelan oil.⁴⁷ Moreover, the national shipping company of Iran set up various businesses made to look like they were separate entities by registering businesses and front companies in offshore jurisdictions including the Isle of Man, Samoa, Hong Kong, Cyprus, China and Turkey.⁴⁸

Manipulating the Automatic Identification Information System (AIS): The AIS is a satellite-based tracking system initially developed to avoid vessel collisions but is now also a useful mechanism to track vessels shipping sanctioned cargo to and from sanctioned countries. Bad actors may manipulate this signal by turning it off to conceal its location. A recent example involving a Cyprus-flagged oil tanker shows the advent of a new AIS manipulation technique. Rather than ‘going dark’ to conduct illicit activities, off-ship agents tampered with the AIS by leaving false tracks and making it appear as if it was in the waters near Dominica while it was really loading oil in Venezuela.⁴⁹ Although this attempt was ultimately unsuccessful because of other factors, it shows that bad actors continue to develop sanction evasion techniques to avoid detection despite advances in technology.

⁴⁶ <https://rusi.org/commentary/flagging-down-north-korea-high-seas>

⁴⁷ <https://www.reuters.com/article/venezuela-oil-uae-specialreport-int-idUSKBN2930YE>

⁴⁸ <https://sayari.com/blog/how-irans-national-shipping-company-used-offshore-companies-to-dodge-u-s-sanctions/>

⁴⁹ <https://apnews.com/article/europe-technology-business-1cd3714c9ce906b8fc931ebb95cb9e26>

Ship-to-ship transfers and voyage irregularities: The practice of ship-to-ship transfers refers to a vessel transferring sanctioned cargo to another vessel at sea rather than at port, often ‘going dark’ simultaneously. The aim of this method is to hide the origin and destination of the cargo. Another method to achieve this is by taking indirect routes or making a transshipment through third countries that are not suspicious. This simultaneously gives an appearance of legitimacy, reducing the risk of detection.

U.S. Real Estate: The real estate sector has long been a preferred vehicle to evade detection and hide ill-gotten gains for a wide range of criminal actors including sanctioned governments, war criminals, kleptocrats, and drug traffickers.⁵⁰ What makes real estate valuable is the ease with which it can be used to hide the identity of the real owners and its ability to not just retain value but also create long-term profits.

The vulnerabilities of the real estate sector are not new but what is concerning is that other comparable jurisdictions like the U.K and Canada⁵¹ exposed to the same risks have in recent years taken stringent action to counter the threat of their real estate sectors being utilized as a haven for ill-gotten wealth. In the U.S. by contrast, regulatory and reporting requirements for the sector are woefully inadequate and appear to have stalled since 2018⁵² and provide an easy mechanism to evade sanctions, gain access to the U.S. dollar and the U.S. financial system.

An often-cited example is the purchase of a New York skyscraper by the Iranian government using a series of shell companies in the U.S and in Jersey to bust through U.S. sanctions.⁵³ The rent from the property was ultimately routed back to Bank Melli and benefited the Iranian government. Yet current U.S. reporting requirements for the real estate sector apply only to residential real estate purchases that are all cash and purchased through a legal entity. The current Geographic Targeting Order (GTO)⁵⁴ rules would not have targeted the “commercial real estate” acquisition by the Iranian government. Similarly, the real estate sector is not just used by sanctioned entities and individuals, the sector provides a convenient way to legitimize the monies obtained by individuals that help governments like Iran and North Korea evade sanctions. In all these cases, the schemes covered U.S. States where the GTOs were not in force like Alaska or utilized the EB-5 investment program which invests in commercial real estate

⁵⁰ Lakshmi Kumar and Kaisa de Bel, *Acres of Money Laundering: Why U.S. Real Estate is a Kleptocrats Dream*, July 2021 (forthcoming)

⁵¹ See note 12

⁵² *Supra* note 49

⁵³ *Ibid*

⁵⁴ [FinCEN reissues Real Estate GTOs targeting 12 Metropolitan areas](#) (April 2021)

in the U.S. which again is not subject to the requirements of the GTOs.⁵⁵ Similarly, Venezuelan officials that were subsequently placed on sanctioned lists were able to move their ill-gotten wealth into U.S. real estate holdings with relative ease and no questions asked about their finances.⁵⁶

Pooled Investment Vehicles: Amongst the entities that are exempt from the requirement to provide beneficial ownership information contained in the provision of the recently passed Corporate Transparency Act are pooled investment vehicles which includes private equity, hedge funds, and venture capital funds. These entities are not required to conduct AML due diligence when accepting funds from investors. A recent leak of FBI documents⁵⁷ revealed that these vehicles were used by drug traffickers, Russian organized crime group, and other transnational organized crime groups to move and hide their illicit finances. The leaked document cites a specific example of use in sanctions evasion schemes. In the example cited a London- and New York based hedge fund proposed “using a series of shell corporations to purchase and sell prohibited items from sanctioned countries to the United States.” The proposed hedge fund was to have operated entities registered in Luxembourg and Guernsey to evade regulatory requirements when transacting with sanctioned companies.⁵⁸

Gatekeepers: Sanctions’ evasion schemes are impossible without a global network of gatekeepers and facilitators that include lawyers⁵⁹, accountants, investment advisers, art advisers⁶⁰, real estate agents, company service providers that employ their knowledge and skills to undermine the very systems their professional ethics dictate they should protect. The ability to tackle sanctions evasion is strengthened if reporting obligations exist at vulnerable points during a financial or trade transaction. Placing the burden on one singular actor like a financial institution ignores the complicit role these actors play in undermining national security, but it also presents opportunity in not creating a reporting obligation at the juncture where the vehicle, channel or scheme is created to evade U.S. sanctions. The U.S. is particularly lagging in this regard. Other G7 countries have started to require gatekeeper CDD obligations for some limited transactions. This even extends to lawyers and notaries when they are involved in real

⁵⁵<https://www.justice.gov/usao-dc/pr/us-files-complaint-forfeit-500000-eb-5-visa-investment-funds-and-over-140000-sanctioned>;
<https://www.wsj.com/articles/chinese-man-tied-to-north-korean-trade-applied-for-u-s-investment-visa-1516900647>;
<https://www.justice.gov/opa/pr/justice-department-seeks-forfeiture-more-20-million-assets-relating-unlawful-use-us-financial>

⁵⁶ <https://www.nbcnews.com/news/latino/u-s-indicts-venezuelan-media-tycoon-ties-maduro-s-government-n938436>

⁵⁷ See note 59

⁵⁸ <https://scientologymoneyproject.com/wp-content/uploads/2020/07/FBI-Intelligence-Bulletin-Threat-Actors-Likely-Use-Private-Investment-Funds-to-Launder-Money-Circumventing-Regulatory-Tripwires2.pdf>

⁵⁹ <https://www.globalwitness.org/en/press-releases/undercover-investigation-american-lawyers-reveals-role-overseas-territories-moving-suspect-money-united-states/>

⁶⁰ <https://www.nytimes.com/2019/12/13/arts/design/art-collector-sanctions-hezbollah.html>

estate transactions. However, in the U.S. these requirements gatekeeper obligations continue to remain wholly absent.⁶¹

The role of FinCEN: While the aim of this testimony has been to focus on the schemes used to evade sanctions, detection of those schemes through the SAR reporting mechanism falls within the purview of FinCEN. As the recent leaks of SAR filings from FinCEN revealed, the constraints around resources have meant that FinCEN is not able to convert SAR reports of possible sanctions evasion into tangible to support law enforcement action. The SARs show that Russian President Vladimir Putin's close friend Arkady Rotenberg is believed to have transferred money to Barclays Bank in London through a company called Advantage Alliance which was subsequently used to purchase vast quantities of art.⁶² Similarly, these leaked files also revealed that sanctions against Syria were also likely to have been circumvented. *“The Bank of New York Mellon is reported to have transferred \$224 million for a company based in Malta called Petrokim.”*⁶³ Investigations indicated that some of the transactions possibly benefited people blacklisted under the Syrian sanctions program. Therefore, at its very crux, mitigating against sanctions evasion schemes requires adopting a two-pronged strategy: addressing the regulatory gaps in the U.S., but also strengthening the institutions responsible for supervision and oversight.

Recommendations

➤ **Strengthen Beneficial Ownership:**

- a. FinCEN should continue to prioritize the implementation of the Corporate Transparency Act and the creation of a robust beneficial ownership registry.
- b. Collecting beneficial ownership information should be extended to all legal forms and arrangements including trusts and to assets such as art, real estate, aircrafts, and boats that are owned through a foreign or domestic legal entity/ arrangement.
- c. The U.S. should champion the establishment of effective beneficial ownership registries internationally including prioritizing the creation of beneficial ownership registers for states that act as ‘flags of convenience’.
- d. The U.S. should (allowing for an appropriate time for implementation) ban any cargo or container ship, tanker or fishing vehicle from entering any U.S. port without first providing beneficial ownership information to Customs and Border Protection

⁶¹ See footnote 7

⁶² *Infra*

⁶³ <https://www.dw.com/en/fincen-files-the-art-of-evading-sanctions/a-55040214>

➤ **FinCEN:**

- a. Ensure that FinCEN has the requisite budget necessary to meet the illicit financial flow challenges facing the U.S. trade and financial system.
- b. Create within FinCEN a National Anti-Money Laundering Academy (NALMA) to establish a credentialled cadre of financial intelligence professionals in the U.S. government, law enforcement, among federal and state prosecutors, and financial institution compliance officers
- c. Create in FinCEN a National Anti-Money Laundering Data Center (NALDC) for advanced data collection, synthesis, analysis, and distribution to law enforcement for AML activity.
- d. Establish a “Manhattan Project” to identify, develop and operationalize state of the art technologies needed to fulfil the technology needs of a NALDC.

➤ **Address Trade-based Money Laundering:**

- a. Establish within FinCEN a permanent “TBML Team” solely focused on studying and identifying TBML threats and conveying that information to appropriate law enforcement.
- b. Advocate for international standards to be created and implemented on TBML similar to AML/CFT. Current FATF 40 recommendations are not fit for purpose to address TBML schemes and only apply to AML.
- c. Require the exchange of trade transaction information between partner countries in a mutually compatible data format. Expand this subsequently to also include the beneficial ownership information of either party to the trade transaction.
- d. Conduct awareness raising and outreach programs on the vulnerabilities of TBML to sanctions evasion and create a relevant set of red flag indicators highlighting the risks of free zones and vulnerable sectors like oil, gold, dual use technologies etc.

➤ **Gatekeeper regulation:**

- a. Real estate sector: Identify the relevant gatekeepers and extend CDD requirements to cover the purchase and sale of all real estate transactions (both commercial and residential) irrespective of value across the United States.

- b. Pooled Investment vehicles: FinCEN should issue rules that require investment advisers to carry out customer due diligence including enhanced customer due diligence on all prospective investors.
- c. Require gatekeeper professions including accountants, lawyers, real estate agents to meet the reporting requirements of the Bank Secrecy Act more fully. For lawyers, these CDD requirements can be limited to transactions that do not breach attorney-client privilege.



GLOBAL FINANCIAL INTEGRITY

1100 17th Street, NW, Suite 505 | Washington, DC | 20036 | USA
Tel. +1 (202) 293-0740 | Fax. +1 (202) 293-1720 | www.gfintegrity.org

President & CEO: Tom Cardamone

**Board: Lord Daniel Brennan (Chair), Dr. Rafael Espada (Vice Chair),
Raymond Baker (Founding President, Treasurer), Dr. Huguette Labelle (Secretary),
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