Iranian Black Market Currency Exchange  

October 2013

“It doesn’t matter if a cat is black or white, so long as it catches mice.”

- Deng Xiao Ping, Paramount Leader, Peoples Republic of China (1904 - 1997)

Ordinary Iranians are paying a heavy economic price for the political transgressions of their leaders. Many are sending their family savings overseas through trade-based money laundering methods normally associated with South American drug cartels. In a variant of the Black Market Peso Exchange (BMPE), capital flight out of Iran is finding innovative ways of circumventing foreign exchange controls, country sanctions and correspondent banking restrictions imposed on Iranian financial institutions.

The BMPE originated in the 1980s to launder the massive amounts of cash generated from the sale of narcotics in the United States. Dollars generated from drug sales would be sold to a broker in the United States. At the same time, Colombian pesos would be sold by a legitimate importer in Latin America to the same broker. The broker would exchange title of the dollars from the drug cartel to the importer, giving the importer hard currency with which to purchase goods for shipment to South American countries. The importer’s pesos would be exchanged for dollars amassed by the drug cartels, as narco-traffickers have operating liabilities in pesos. The broker, trusted by all parties, would earn a commission for arranging the transaction.

In a BMPE, no currency crosses borders, only title to a stash of cash or a highly negotiable instrument denominated in one of the currencies. Bank drafts are the traditional negotiable instrument, however some parties in a BMPE will pay a premium to acquire funds deposited in a financial institution, the cleanest money that dirty money can buy. The BMPE has been described by the American financial intelligence unit, FinCEN, as “...the single most efficient and extensive money laundering ‘system’ in the Western Hemisphere”\(^1\). Estimates on the annual amount of dirty money washed by the BMPE typology run into the billions\(^2\).

Modern variants suggest that organised crime is actually getting involved in the business of international trade to sanitise illicit funds and move value around the world. The January 2013 issue of ManchesterCF Analytics\(^3\), entitled “Black Market Trade Exchange”, outlined how organised crime is

\(^2\) http://www.pbs.org/wgbh/pages/frontline/shows/drugs/special/blackpeso.html
\(^3\) Contact ManchesterCF for a copy of this issue – info@manchestercf.com
moving up the value chain in international trade. Firms controlled by organised crime are able to
open letters of credit, make global payments and deal in a wide variety of goods around the world.
For financial institutions defending themselves against money launderers, this level of sophistication
cause for concern. The BMPE is no longer about the exchange of dollars and pesos, as it now
includes the actual trade in goods overseas by seemingly legitimate enterprises.

A major international bank recently described to ManchesterCF a new development in the BMPE
typology that adds another dimension of complexity. Payment transaction monitoring software at the
bank revealed a transfer of funds from a trading company overseas into the personal account of a
recent immigrant from Iran now residing in a G7 country. Bank policy dictated that a payment from
an overseas trading company into a new personal banking account is cause for further enquiry.

The individual holding the personal bank account was very forthcoming. Having just sold their family
home in Iran, they needed to get the funds out of the country and into their new life abroad. The
traditional route of wiring the proceeds from the house sale directly to their new bank account was
impossible, as sanctions against Iranian banks prevent such direct payments. Such a payment would
have nothing to do with proliferation or terrorist financing, yet it can be blocked by legislation and
regulations enacted by countries to place economic pressure on Iran.

Currency sanctions are never completely effective, as enterprising brokers will find a way to create
payment mechanisms that circumvent rules and regulations imposed by governments. Capital flight
out of China through fake invoicing for non-existent exports was estimated at USD75-billion for the
first four months of 2013. Currency restrictions on South American currencies in the 1980s were one
of the principal driving forces behind the creation of the BMPE. The South African rand and
Malaysian ringgit have had porous restrictions imposed by national governments.

By tearing a page out of the BMPE playbook, brokers in Iran and offshore financial centres are able to
match sellers of Iranian riyals with sellers of hard currencies overseas. Matching Iranian exporters
with individuals seeking ways of sending their savings out of Iran creates a currency market for the
broker. As this currency market must operate outside of the reach of financial institutions adhering to
Iranian sanctions regulations and regulators attempting to enforce the regulations, it is a black market
currency exchange that reaches across international borders.

Iranian exporters of oil, dates, textiles and other goods are able to ship their goods overseas but face
difficulties when invoicing their customers. They must often employ middlemen throughout the
Middle East and often Asia to front for their transactions. Avoiding USD is key, as the strongest
ponent of Iranian economic sanctions is the United States. Other countries that issue hard
currency, including Canada, Australia and the European Union place restrictions on Iranian financial
institutions, individuals and corporations dealing in their respective currencies.

International financial institutions based in these countries offering correspondent banking services to
respondent banks around the world are very curious about their respondent banks dealing with Iranian
ties directly or entities covertly representing sanctioned Iranian individuals, corporations or
financial institutions. A tremendous amount of time and effort is expended by major
correspondent banks to ensure they don’t become unwitting conduits for sanctioned
entities via their respondent banks.

The Iranian export transaction is constructed so that the buyer’s funds are directed to a trading
company in an offshore financial haven, such as Dubai or Hong Kong. The trading company will

4 http://in.reuters.com/article/2013/06/14/china-economy-fake-trading-idINDEE95D02520130614
5 http://www.pbs.org/wgbh/pages/frontline/shows/drugs/special/blackpeso.html
6 http://www.xe.com/currency/irr-iranian-rial
arrange to negotiate letters of credit issued by the buyer’s bank for the Iranian goods. Proceeds from the letter of credit are then deposited at the trading company’s corporate banking account in the offshore financial centre.

The Iranian immigrant wishing to transmit funds overseas in hard currency will make a local bank payment or cash delivery to an Iran-based broker. This broker contacts the trading company in the offshore financial centre, notifying them that the Iran-based broker has possession of riyals in exchange for hard currency.

The trading company quotes a price for the hard currency it has on hand from the export sale and a deal is struck. The Iranian exporter receives payment for their shipment in riyals, courtesy of the Iran-based broker. The recent Iranian immigrant located in a G7 country is notified by the trading company that their hard currency is ready for delivery, often requesting they supply the individual’s retail banking account number, branch address and SWIFT Bank Identification Code (BIC).  

A short while later, the Iranian immigrant sees their G7 currency bank balance swell for an amount almost equivalent to the funds they wanted transmitted out of Iran, as various commissions will be paid to the middlemen facilitating the transaction.

On the other side of the planet, the Iranian trading company is boosting its cash flow figures by an amount almost equivalent to the proceeds from their export sale, and in local currency. Management will be pleased that onerous foreign trading restrictions have been avoided and will most likely engage in similar transactions. Management could expect possible retribution if prosecuted by local authorities, however the successful completion of an export transaction will temper any reaction.

Currency did not flow across borders, only title. The Iranian immigrant building their new life in a G7 country never committed any crime, nor was involved in terrorist financing or weapons proliferation. If the Iranian exporter is privately held with an arms-length relationship to the national government, its shipment did not weaken the defence of any nation nor cause anyone any direct harm.

If the Iranian trading company was owned by the state or a sanctioned corporation, financial institution or individual, the transaction becomes fraught with risks, compliance issues and investigations of money laundering, terrorist financing and the proliferation of weapons of mass destruction. For the lonely money laundering analyst sitting at a desk in the City of London, on Wall Street, on Bay Street, in Central or in Raffles Place, sifting through such probabilities is not for the inexperienced, nor the timid.

In 2013, ManchesterCF partnered with the International Compliance Association (ICA) to provide a Specialist Certificate in trade-based money laundering. The Certificate is based on ManchesterCF’s Financial Crime Training (Trade-based money laundering) program for financial institutions, financial intelligence units and public-sector agencies. Please visit the ICA website for further details.

ManchesterCF provides financial crime risk management training programs, advisory services and project management to financial institutions and public-sector agencies around the globe.