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British Bank Accused of Doing Massive Illegal Iran Business: Settles with New York Authorities

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On August 6, 2012, the New York State Department of Financial Services (DFS), the state banking regulator, [accused](#) Standard Chartered Bank (SCB) of Britain of using its New York state branch as a clearinghouse for Iran transactions in a massive cover-up scheme involving at least \$250 billion. The DFS stated in an [order](#) that in review of 30,000 pages of bank documents and e-mail communications, it found that for nearly ten years, SCB officials “programmatically engaged in deceptive and fraudulent misconduct,” concealing transactions with Iranian financial institutions including its Central Bank/Bank Markazi, Bank Saderat, and Bank Melli, which are affiliated with Iran’s nuclear and missile programs. The bank was also accused of transacting with other sanctioned countries.

On August 14, SCB [settled](#) with the DFS and agreed to pay \$340 million for the alleged violations. SCB maintained that only \$14 billion of the \$250 billion in transactions in question were illegal. It reportedly decided to settle to avoid a DFS hearing on August 15 to determine whether to revoke its New York State operating license, further reputational damage, and additional declines in its share price. The settlement is a reversal for Standard Chartered which issued a press release last week [rejecting](#) the DFS’s portrayal of its activities. It will [acknowledge](#) misconduct in the settlement.

This case has involved bureaucratic differences over the DFS choosing to move on the case on its own rather than in concert with federal and district authorities. At issue is also whether pre-2008 transactions were violations of U.S. law, which at the time allowed foreign banks to clear payments from Iran in dollars. SCB nonetheless did not report the Iran transactions, and in doing so thwarted money laundering investigations, the DFS alleged. The Treasury Department, Federal Reserve, and Manhattan District Attorney are still investigating the matter. The Justice Department has not yet determined whether to pursue a criminal case.

The Alleged Scheme

From 2001 until 2007, the DFS alleged that Standard Chartered Bank conspired with Iranian clients to strip information from SWIFT wire transfer messages, a practice termed “wire stripping,” to conceal the origin of more than 60,000 transactions from Iranian banks made through its branches. The DFS’s order claimed that SCB ensured anonymity of the transactions by systematically screening and removing or replacing with false entries information in messages containing any indication that the client was Iran. Roughly half of the 60,000 transactions were made from Iranian banks through SCB’s London headquarters and the other half went through its Dubai branch to the New York State branch. Its New York State branch would then clear the payments in dollars, a process called “U-turning.”

The bank allegedly claimed in internal memoranda that it was doing its own job of due diligence and the U.S. Treasury Department Office of Foreign Assets Control's (OFAC) job of screening transactions on an "offshore" basis, i.e., stripping the obvious information in wire messages to conceal the Iranian origin before they went through its branch in the United States. The U.S. Treasury Department requires any bank doing business in the United States to screen, freeze, and report attempted or suspicious transactions made by Iranian entities. The DFS order rejected the bank's claims, stating that SCB hindered money laundering investigations against Iran and withheld information from U.S. regulators even, egregiously, while under formal investigation for other compliance failures, and covered up its activities for years, making it a "rogue institution."

In one 2006 e-mail communication cited by the DFS investigation, SCB's CEO of the Americas wrote to the Group Executive Director in London that the Iran dollar-clearing program needed review "to evaluate if its returns and strategic benefits are...still commensurate with the potential to cause very serious or even catastrophic reputational damage to the Group." The executive underscored the potential for criminal liability. The director, in response, communicated in caustic language that America could not dictate whether the rest of world could do business with Iran. By contrast, the order highlighted, SCB states on its website that it prides itself on being "trusted worldwide for upholding high standards of corporate governance" and on its "moral compass."

According to the order, SCB allegedly ran this program specifically as part of an effort to secure more Iran business, an effort it termed "Project Gazelle" in internal memoranda. In one memo circulated among SCB's legal, compliance, and Iran client managers, SCB's CEO for the UAE and its Group Head of Compliance and Regulatory Risk wrote that SCB's "short to medium term strategy [was] to grow the wholesale business by growing our wallet share from existing relationships with Financial Institutions and Iranian companies and establishing new relationships with Iranian companies and [intermediaries] in oil and gas related business." It appears that SCB's alleged project finally backfired.

Lessons and Observations

This case shows that U.S. efforts to leverage its position in the global economy against Iran by punishing and uncovering sanctions violations by banks is increasingly hurting Iran's ability to do business. Iran continues to require access to the U.S. financial system to process payments in dollars and seeks willing banks to help it do so in violation of U.S. law. This case shows that Iran's ongoing efforts to access the U.S. financial system, including paying for needed goods illicitly procured for its nuclear and missile programs, provide ample opportunities for U.S. authorities to track and monitor Iran's efforts and stop this activity. Authorities can also learn more about Iran's illicit procurement efforts and pinpoint new entities to sanction.

This case shows that U.S. efforts against noncompliant banks, over time, should create a principle of deterrence for financial institutions with operations in the United States. The major fines that the United States has commanded in these recent investigations underline the importance of banks being able to do business with the U.S. economy and operate branches in New York State. Not counting the recent settlement with Standard Chartered, the U.S. government and New York State investigations into violations of U.S. sanctions against Iran have thus far netted more than \$2 billion in penalties. Banks found to be in noncompliance and fined with operations in the United States include Barclays, ING, Credit Suisse, Lloyds, and ABN Amro. HSBC is also under investigation. The reputational damage

wrought by a noncompliance scandal has at least temporary [impacts](#) on financial institution shares and earnings, as seen by a 20 percent slide in SCB's shares following news of the investigation, its [largest slide](#) in 24 years. Criminal liabilities can extend this reach even further. In the years to come, the alleged activities of banks such as Standard Chartered should become relics of the past.

Nonetheless, the fact that SCB was allegedly able to conceal this massive amount of business brings into question the effectiveness of current U.S. regulatory efforts. U.S. federal regulators must vigorously pursue investigations and prosecutions and improve measures to uncover such noncompliance activities to ensure that banks no longer have the opportunity to hide illegal Iran business. Some banks also process Iran transactions inadvertently due to Iran's clever concealment mechanisms. The U.S. government must work closely with bank compliance departments to ensure they are up to date on the latest Iranian schemes which aim to conceal the origin of transactions through the U.S. financial system. Financial institution screening systems will never be able to catch all of Iran's illicit transactions, but authorities can help them target their due diligence efforts to stop more and be more effective.

This case shows that as U.S. and international sanctions efforts against Iran are augmented, Iran's costs and difficulty of doing business are also increasing, part of a coordinated global effort that will hopefully put more pressure on the regime and convince it to change its nuclear policies.