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How Cooperation between a Company and Government Authorities Disrupted a Sophisticated Illicit Iranian Procurement

By David Albright, Paul Brannan and Andrea Scheel

Following tips from a European intelligence agency, a European company discovered a new strategy used by Iran to circumvent export controls, in this case a clever scheme to obtain vacuum pump systems for its centrifuge program. The elaborate ruse involved a Chinese manufacturing company with an established relationship with the European company. In early 2006, this company received a tip from a friendly European government to be on guard for enquiries from Saudi Arabian companies for certain types of pumping systems that would be diverted to Iran. The company did not receive such an enquiry, but its South Korean daughter company did receive a similar enquiry from an entity wanting to ship such items to Iran. The company refused this enquiry.

Several months later, the European intelligence agency asked the European company to look into a recent order placed by a Chinese company. After reviewing enquiries and contracts, the company soon found that the Chinese company had ordered 15 such pump systems, seven of which the company had already delivered to the Chinese company via the European company's Chinese subsidiary. The Chinese company, an established manufacturing company, called an "original equipment manufacturer" (OEM), had ordered the pumps as part of a larger order it had received to build oil purification equipment for electrical power plants. The supplier did not need its government's approval to supply the pumps; the sale did not require a license and was not overtly suspicious. The Chinese company had not previously been associated with illicit activities. After the discovery, company officials from the European supplier immediately contacted the Chinese company and asked for the end user of the equipment. The Chinese company official was vague. He said that the vacuum equipment, including the pump systems, were for an overseas customer, and in fact the firm had already exported the seven pump systems, but he refused to reveal the customer. The European company stopped any further shipments of pumps to this company. The Chinese company demanded the rest of the pumps or all its money back. Then, it cancelled the order, perhaps to prevent having to admit at some stage that its customer was Iran.

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236 Massachusetts Avenue, NE, Suite 500 Washington, DC 20002

TEL 202.547.3633 • FAX 202.547.3634

E-MAIL isis@isis-online.org • www.isis-online.org

European government authorities were notified, one of which learned from the Chinese government that the pumps did indeed go to Iran. Although they did not learn the exact end user, they believed Iran's centrifuge program was the likely customer. Figure 1 shows the relatively short, but hard-to-detect, procurement network involved in this scheme.

No prosecution was launched against the European company for its export of pumps. Instead, the intelligence services applauded the European company's cooperation to uncover this dangerous new Iranian scheme. The governments' attitude was that companies should not be punished for exercising good citizenship.

Figure 2, from a report released by the Financial Action Task Force (FATF)¹, depicts the growing complexity of illicit procurement schemes over time. The first model is a direct sale from a supplier to a proliferant state program, followed by increasingly deceptive models involving procurement organizations fronting for the proliferant state program and trading companies that further hide the true end user. In the model circled in red, a manufacturing company sells goods to a second manufacturer, who then sells the product to an end user which was never declared to the first manufacturer. This last model closely resembles the tactic which involved the Chinese manufacturer. Whereas suppliers have historically been on the look-out for being targeted in illicit procurement schemes involving only trading companies, they must now be increasingly on alert for illicit networks incorporating legitimate manufacturers.

This case highlights the importance of governments cooperating with companies on suspected illicit procurement attempts. If the European authorities had not contacted the European supplier, the supplier would have never known that the vacuum pumps were sent to Iran and likely ended up in its gas centrifuge uranium enrichment program. Even the best internal compliance system cannot detect these types of illicit procurement, and cooperation between government and industry is necessary in order to prevent these smuggling networks from succeeding.

¹ <http://www.fatf-gafi.org/dataoecd/14/21/41146580.pdf>

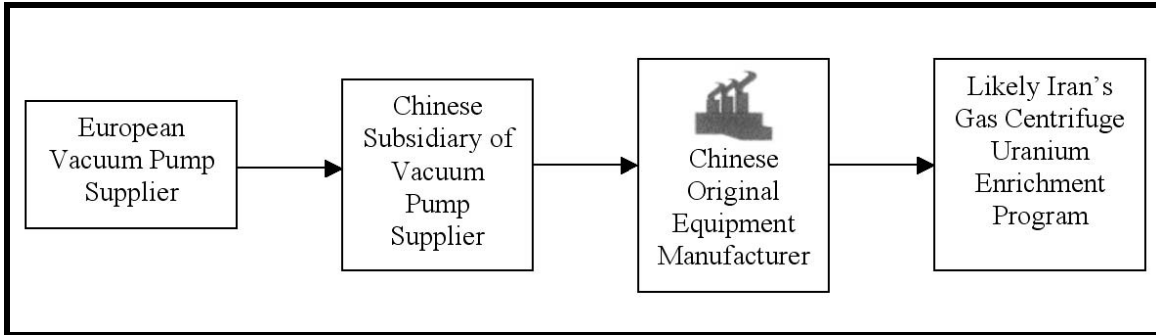


Figure 1. Diagram showing the vacuum pumps sold to Chinese manufacturer from European supplier. The Chinese manufacturer then sent the pumps to Iran where it is believed they were utilized by Iran’s gas centrifuge program.

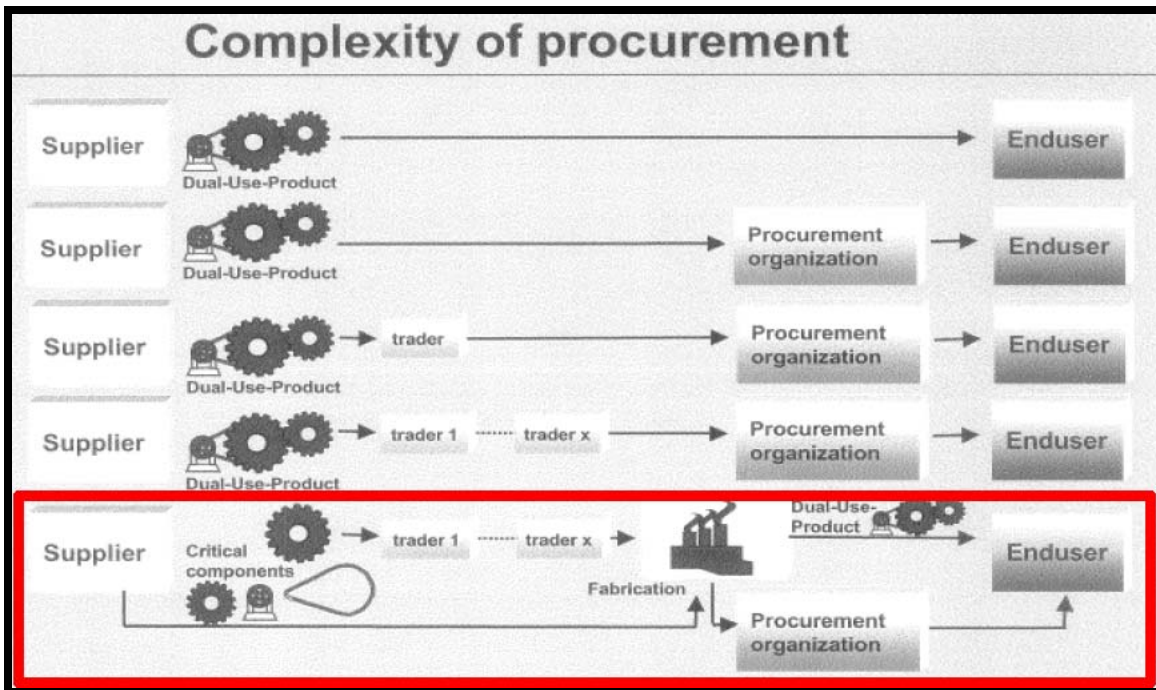


Figure 2. Diagram from the *Proliferation Financing Report* released by the Financial Action Task Force (FATF). The diagram depicts different methods of illicit procurement. The example of illicit procurement highlighted in red, closely resembles the method used by Iran which employed the Chinese manufacturer—represented in the diagram as “Fabrication”.