

June 8, 2012

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**Re: Lebanese Sovereign Bonds/Your Investment in Lebanese Sovereign Bonds and Related Securities/Lebanon Operates as a Sovereign Money Laundering Enterprise/The Fraudulent Scheme to Support Lebanon's Sovereign Backed Securities/The Role of Institutional Lebanese Sovereign Bond and CDS Holders**

Dear Mr. Cracchiolo:

The purpose of this letter is to place you on notice of our grave concern related to certain Lebanese sovereign backed and related securities that you (apparently) hold in portfolio and to call upon you to divest from all Lebanese sovereign backed debt securities that you may hold. According to record information from Bloomberg, Riversource Investments LLC may hold significant amounts of such securities.<sup>1</sup>

For some time, United Against Nuclear Iran ("UANI") has been investigating the role of Hizballah, Iran and Syria in the Lebanese banking system ("LBS"). As part of this investigation, we have relied on both public and confidential sourcing. UANI has been corresponding with and making inquiry with the central bank of Lebanon, Banque du Liban ("BDL") and its governor, Riad Salamé. As a product of that correspondence and investigation regarding the insidious role of Hizballah, Iran and Syria in the LBS, UANI has revealed that Lebanon is a sovereign money laundering operation that enables Lebanon to support a fraudulent market for its sovereign bonds.

Simply put, the value of Lebanese sovereign bonds and related securities is based on a massive fraud.

Attached for your review is our most recent correspondence with Governor Salamé, which includes an economic analysis of Lebanon's sovereign debt. The correspondence and

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<sup>1</sup> Bloomberg L.P. Lebanese sovereign bond holdings. Bloomberg terminal, March 30, 2012.

UANI's presentation reveal a sovereign money laundering scheme that creates a fraudulent sovereign debt market.<sup>2</sup>

By this letter, UANI calls on you and all Lebanese sovereign bond and credit default swap ("CDS") holders to divest all such securities that are, of course, far riskier in nature than they appear on their surface in order to ensure that you do not unwittingly support Lebanon's role as a sovereign money launderer and its sovereign debt fraud.

Our analysis reveals that as a result of the actions and omissions of BDL and the LBS, Lebanon has become a sovereign money laundering jurisdiction that receives massive inflows of illicit deposits. Those illicit monies are generated from Hizballah terror and criminal activities, and the illicit symbiotic relationships among Iran, Syria and Hizballah that is founded on terrorism, the material support of terrorism, and weapons transfers, including as related to weapons of mass destruction. Building upon a foundation of such massive inflows of illegitimate monies, Lebanon has portrayed a false image of economic legitimacy and stability to global markets, particularly as related to its sovereign bonds and related securities including the CDS that "insure" those bonds. In fact, the real picture of Lebanon and its sovereign backed securities reveals a fraud and market manipulation that is used by Hizballah, BDL and the LBS to continue money laundering on a massive scale. We believe that BDL and the LBS meet the criteria for determination under Section 311 of the USA PATRIOT Act of 2001 ("USA PATRIOT Act") as a jurisdiction of primary money laundering concern that would result in their ban from the U.S. financial system.

As you know, Hizballah remains "the most prominent and powerful terrorist group in Lebanon.... The Lebanese government continue[s] to recognize Hizballah ... as a legitimate 'resistance group' and political party."<sup>3</sup>

[Hizballah] receives training, weapons, and explosives, as well as political, diplomatic, monetary, and organizational aid from Iran; training, weapons, diplomatic, and political support from Syria; and funding from private donations and profits from legal and illegal businesses.<sup>4</sup>

Hizballah is as strong as ever having rearmed after the 2006 war.<sup>5</sup> However, Hizballah has diversified its income to supplement the money that it receives from Iran.

Hizballah is now heavily involved in a wide range of criminal activity, including the drug trade and smuggling.<sup>6</sup>

Hizballah's network of financial support knows no borders, with active operations in many places around the globe, including Africa, the Middle East, Europe and

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<sup>2</sup> See attached Exhibit A

<sup>3</sup> U.S. State Department, [Country Reports On Terrorism 2010](#) (September 18, 2011).

<sup>4</sup> [United States of America v. Lebanese Canadian Bank SAL, et al.](#), 11 Civ. 9186, at p. 17 (December 15, 2011).

<sup>5</sup> Testimony of Feltman and Benjamin (June 8, 2010).

<sup>6</sup> [USA v. LCB, et al.](#) at 19.

Latin America.<sup>7</sup> The United States, European Union and others have sanctioned various affiliates of Hizballah for their support of terrorist activities and the financing that supports Hizballah's activities. The United States has taken steps to sanction "Bayt al-Mal and the associated Yousser Company, which together function as Hizballah's unofficial treasury, holding and investing its assets and serving as intermediaries between Hizballah and the mainstream banks."<sup>8</sup>

Hizballah's illicit support in cash and cash proceeds from criminal activities are systematically generated in and/or transferred to Lebanon. "The cash is often moved through bulk cash smuggling.... Hizballah members and supporters facilitate the smuggling of cash."<sup>9</sup> The recent civil forfeiture proceeding brought by the U.S. Attorney for the Southern District of New York against the Lebanese Canadian Bank ("LCB") and related parties detailed a stunningly open system for the criminal smuggling of cash into Lebanon. The LCB Complaint describes the Beirut International Airport as a cash smuggling hub for Hizballah.

In February of 2011, the U.S. Attorney for the Southern District of New York in the matter of United States v. Maroun Saade, et al. brought attention to a cocaine and heroin smuggling operation that involved the Taliban and Hizballah. Among the startling information contained in this action was its reference to the large scale cash smuggling operation into Lebanon.<sup>10</sup>

Of course, illicit cash inflows into Lebanon require laundering and deposit into the LBS for Hizballah to effectively manage and deploy such monies across its global web of associates. The LCB Complaint details the willingness of the LBS (in this case LCB) to receive large scale cash deposits with no questions asked. The LCB Complaint describes such cash deposits including up to \$200,000.00 per day at certain branches of the LCB.<sup>11</sup>

Iran's role in Hizballah is no secret, but just in February of this year did Hizballah's leader Hassan Nasrallah acknowledge that Hizballah was financially supported by Iran.<sup>12</sup> That support is reported to be at least hundreds of millions of dollars per year and we believe much more based on the information contained herein.<sup>13</sup> Iran's support is the keystone by which Hizballah has built its dominant presence in Lebanon and avoided the economic stranglehold of U.S. and EU sanctions. "Of course, one cannot hope to apply effective financial pressure against a group like Hizballah so long as it maintains massive inflows of cash from a state sponsor of terrorism, in this case the Iranian Government."<sup>14</sup>

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<sup>7</sup> Id.; [The New York Times](#), "U.S. Sues Businesses It Says Helped Hezbollah," (December 15, 2011); [CBC News](#), "Argentina Charges Iran, Hezbollah of 1994 Jewish Centre Attack," (October 25, 2006); [BBC News](#), "Iran Charged Over Argentina Bomb," (October 25, 2006); [Los Angeles Times](#), "Fears of Hezbollah Presence in Venezuela," (August 27, 2008); [Remarks](#) by Robert M. Morgenthau at the Brookings Institution (September 8, 2009); [Testimony](#) of Douglas Farah, Senior Fellow at the International Assessment and Strategy Center and Adjunct Fellow at the Center for Strategic International Studies, Senate Subcommittee on Western Hemisphere, Peace Corps and Global Narcotics Affairs (February 16, 2012).

<sup>8</sup> [Testimony](#) of Adam J. Szubin, Director, Office of Foreign Assets Control, U.S. Department of the Treasury Before the Senate Committee on Banking, Housing and Urban Affairs (September 12, 2006).

<sup>9</sup> USA v. LCB, et al. at 3.

<sup>10</sup> United States of America v. Maroun Saade, et al., 11 Cr. 111, (February 14, 2011).

<sup>11</sup> USA v. LCB, et al. at 31.

<sup>12</sup> [Hurriyet Daily News](#), "Iran funds Hezbollah, leader Nasrallah admits," (February 9, 2012).

<sup>13</sup> [Foreign Affairs](#), "Hezbollah: Party of Fraud, How Hezbollah Uses Crime to Finance its Operations," (July 27, 2011).

<sup>14</sup> [Testimony](#) of Adam J. Szubin (September 12, 2006).

Just recently, the international press trumpeted the proud role that Iranian financial supports plays in Hizballah's Lebanon.

Iranian largess helped to rebuild neighborhoods flattened six years ago by Israeli bombs an achievement that was commemorated this month with a rollicking celebration. "By the same means that we got weapons and other stuff, money came as well," the Hezbollah leader, Hassan Nasrallah, exclaimed to roars of approval from the crowd. All of this has been achieved through Iranian money!"<sup>15</sup>

Iran's eagerness to shower money on Lebanon when its own finances are being squeezed by sanctions is the latest indication of just how worried Tehran is at the prospect that Syria's leader, Bashar al-Assad, could fall....

Iran's ardent courtship of the Lebanese government indicates that Tehran is scrambling to find a replacement for its closest Arab ally, politicians, diplomats and analysts say. It is not only financing public projects, but also seeking to forge closer ties through cultural, military and economic agreements.

Hezbollah has developed into being a beachhead of Iranian influence not only in Lebanon, but on the Mediterranean trying to spread Iranian culture, Iranian political domination and now an Iranian economic presence, Mr. Hamade said.

"The Iranians say, 'If you want factories, I am ready, if you want some electricity, I am ready,' and they do not ask for any price in return," said Hassan Jishi, the general manager of Waad, the organization that rebuilt the southern suburbs. (The name means "promise" in Arabic, referring to Mr. Nasrallah's promise to reconstruct the area.) It cost \$400 million to build apartments and stores for about 20,000 people, Mr. Jishi said.

Half the money came from Iran, Mr. Nasrallah said in his speech....

"We owe a special thanks to the leaders of the Islamic republic of Iran, to the government, to the people, because without Iranian funding, we could not even have begun to achieve what we did," Mr. Nasrallah said....<sup>16</sup>

Given the large-scale nature of the illicit finances that support Hizballah from Iran's backing and the inflow of other illicit funding, the transacting of that support has to be facilitated by financial institutions – Lebanese banks. Ultimately, the vast majority of these illicit funds are laundered by Bayt al-Mal, Hizballah supporters, front companies and businesses into the Lebanese financial system including and primarily its banking system.<sup>17</sup> But what was once a mechanism for providing financial support for Hizballah has also become a symbiotic financial relationship that allows Iran to evade the growing crush of international sanctions and the

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<sup>15</sup> [The New York Times](#), "Iran Is Seeking Lebanon Stake as Syria Totters," (May 24, 2012).

<sup>16</sup> [Id.](#)

<sup>17</sup> See [infra](#) section "Hizballah Monies Laundered into Lebanese Sovereign Bonds."

possible loss of its brutal ally, Bashar al-Assad in Syria.<sup>18</sup> Now, the Lebanese banking system also provides the means by which Iran transacts funds transfers to ensure the dependability of its Hizballah proxy in order for Iran to evade the effects of sanctions and the growing international banking blockade against the regime.

By traditional economic indicators, Lebanon's economy is in shambles. Lebanon suffers from an extraordinarily high level of debt and extremely high debt to GDP ratio.<sup>19</sup> For example, while Lebanon's GDP is around \$40 billion, roughly equivalent to Uruguay, Lithuania, Costa Rica or Ghana, its sovereign debt is \$53.8 billion – the fourth largest debt to GDP ratio (137% as of December 2011) in the world.<sup>20</sup> The obvious risk of sovereign default is great – unless there is a fraudulent hidden scheme driven by Hizballah and its state sponsors, Iran and Syria, to support this economic house of cards. There is exactly such a scheme.

Lebanon has consistently struggled to service its debt as the country's underlying growth continues to decline.<sup>21</sup> Lebanon has struggled to no avail to reduce its budget deficit, which is particularly difficult given its large trade deficit.<sup>22</sup> Compounding these difficulties is Lebanon's underlying growth is in decline.<sup>23</sup> As a result of all these factors and others such as Lebanon's tenuous politics, credit rating agencies are skeptical of Lebanon – but not skeptical enough. By way of example, Moody's rates Lebanon B1.<sup>24</sup> Countries with similar bond credit ratings to Lebanon have higher sovereign bond yields and higher CDS yields, demonstrating a higher risk of sovereign default.

Yet, Lebanon incongruously supports a stable and outsized banking system and sovereign debt market. Lebanon's historic cost of debt has previously been much higher than it is currently. Lebanon's cost of debt in 2006 and 2007 was much higher (approximately 9%) than it is today (between 5% and 6%).<sup>25</sup> Despite these adverse economic issues, Lebanon's sovereign bonds trade at tight spreads. Lebanese sovereign bonds trade at high cash prices reflecting spreads even lower than applicable CDS<sup>26</sup> spreads<sup>27</sup> with no rational economic explanation – except because of the backing of the money laundering described herein. Lebanese sovereign bond related CDS trade at very low premiums that are difficult to justify.<sup>28</sup>

The irrational strength of Lebanese sovereign bonds corresponds with same time period of increased sanctions pressure against Iran. Iran has sought to avoid sanction pressure by directing more and more support to Hizballah to ensure the stability of its key proxy, and to ensure a financial outlet. Coupled with Hizballah's criminal activities (and the flight of some

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<sup>18</sup> [The New York Times](#) (May 24, 2012).

<sup>19</sup> See Attachment Exhibit "C" in Ex. "A" at 8.

<sup>20</sup> *Id.* at 9.

<sup>21</sup> *Id.* at 10.

<sup>22</sup> *Id.* at 11-12.

<sup>23</sup> *Id.* at 13.

<sup>24</sup> *Id.* at 15.

<sup>25</sup> *Id.* at 16.

<sup>26</sup> According to Bloomberg, credit default swaps ("CDS") are a financial swap designed to transfer the credit exposure of fixed income products between the parties. The buyer of a CDS receives credit protection and the seller of the swap guarantees the credit worthiness of the debt security.

<sup>27</sup> See Attachment Exhibit "C" in Ex. "A" at 17.

<sup>28</sup> *Id.* at 18-19.

capital from Syria), the result is vast inflows of deposits into the LBS.<sup>29</sup> As a result, with all economic indicators pointing to a serious risk of sovereign default, Lebanon's currency and banking system act like the currency and banking system of a far more successful sovereign.

Notably, the illicit Hizballah cash inflows into Lebanon have been gradually increasing coincidental with the rise of sanctions against Iran and as Syria falters.<sup>30</sup> Once laundered into the LBS as bank deposits, the Lebanese banks pay relatively high interest rates and the deposits have to be put to work by the LBS to earn income for the banks.<sup>31</sup> Among other illicit activities, the LBS utilize these deposits to purchase Lebanese sovereign bonds. The LBS's large-scale purchases of Lebanese sovereign debt effectively price support and stabilize what would otherwise be a far more volatile security. The market effect is that Lebanese sovereign bonds and its central banking system are artificially stabilized.<sup>32</sup> Given the size of this financial support, such support can only come from either or both of illicit activities and a state actor – namely Iran.

Lebanon uses the massive cash inflows of criminal funds and Iranian support to fraudulently prop up Lebanon's struggling economy and to manipulate the market for its sovereign debt and the securities that "insure" that debt. Simply put, Hizballah cash is laundered into the LBS, whose institutions purchases Lebanese sovereign debt, thereby manipulating the yield on such securities to appear far more stable and resistant to default. Lebanese sovereign bonds (and related CDS) are a product of a sovereign money laundering scheme.<sup>33</sup>

Based on the foregoing, the LBS can no longer be seen as a legitimate and independent banking system. The LBS is a fraud. Though the Lebanese banking system was once a great and well regarded sovereign banking system, it has evolved into a state-sponsored money laundering enterprise that enables the hidden large scale infusion of criminal and Iranian funds into Lebanon. The focal point of the fraudulent Lebanese banking system centers on BDL.

As you know, Lebanese sovereign bonds are offered as a security for sale in the United States subject to the rules of the United States as well as other jurisdictions where such debt is offered. The manipulation of Lebanese sovereign-backed securities and their fraudulent underpinnings violates a variety of U.S. securities laws.

We believe that based on our analysis and other acts and omissions, BDL and the LBS have been systematically perverted for the benefit of Hizballah and its state sponsors, Iran and Syria. Pursuant to Section 311 of the USA PATRIOT Act, Title 31, United States Code, 5318A, the overwhelming evidence supports the conclusion that, because of the actions of BDL and the LBS, many of the institutions operating within the LBS are money laundering concerns and, because of the pervasive influence of Hizballah, Lebanon is a jurisdiction of "primary money laundering concern" that would require the United States to impose "special measures." Under the terms of Section 311, such "special measures" should include the "fifth special measure" that

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<sup>29</sup> *Id.* at 22.

<sup>30</sup> *Id.* at 23-25.

<sup>31</sup> *Id.* at 22-25; According to [BDL](#), Lebanese commercial banks' savings accounts have an interest rate of 2.59% and checking and current accounts have an interest rate of 0.91% (March 2012).

<sup>32</sup> *Id.*

<sup>33</sup> *Id.* at p. 26.

would prohibit any U.S. financial institution or agency from maintaining correspondent accounts on behalf of a or all Lebanese institution(s).<sup>34</sup> Simply put, under the terms of the USA PATRIOT Act, significant elements of the LBS including BDL, if not Lebanon itself, should be cut-off from the United States financial system. When considering the “fifth special measure,” important factors that must be considered include the national security concerns of the United States. Clearly, taking action to inhibit the pernicious relationship between Iran and Hizballah is a compelling national security interest. Importantly, the impact of a Section 311 jurisdiction determination would have little impact on U.S. institutions and the systemic impact of such action would be of modest effect relative to the important national security interests at stake.<sup>35</sup>

As a result of the foregoing, all holders of Lebanese sovereign debt and related securities should divest their ownership of such fraudulent securities.<sup>36</sup>

Please be advised that UANI does not call for your divestment lightly. We do not seek to harm any legitimate financial institution. Nonetheless, as a result of our investigation and the nefarious scheme it revealed related to Lebanon’s debt market, we felt compelled to notify you and to publicly call for your divestiture of such securities.

UANI seeks your immediate action to divest from Lebanese sovereign backed securities. Institutions engaged in the buying and selling of Lebanese bonds help legitimize this debt instrument as a serious and legitimate investment and support the massive Lebanon/Hizballah/Iran sovereign money laundering scheme. By choosing to invest and/or hold Lebanese bonds, institutions facilitate the nefarious relationship by and between Hizballah, Lebanon, Iran and Syria. Firms can no longer justify holding these bonds and their corresponding CDS, which are a product of a sovereign money laundering enterprise and are artificially propped up by a fraudulent economy. Such investments are too risky and perpetuate the fraud.

Please let us hear from you on or before the close of business on June 19, 2012 concerning your decision to divest from Lebanese sovereign backed securities.

Thank you for your immediate attention to this matter.

Very truly yours,



Ambassador Mark D. Wallace

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<sup>34</sup> [31 U.S.C. 5318A](#)(b)(5).

<sup>35</sup> See Attachment Exhibit “E” in Ex. “A” which is an analysis of the “relevant factors” and “specific factors” to be considered in relation to a Section 311 determination as to Lebanon.

<sup>36</sup> *Id.* at 29 for a list of American holders of Lebanese sovereign debt.

cc: The Honorable David Cohen  
Under Secretary for Terrorism and Financial Intelligence, U.S. Department of the  
Treasury

The Honorable Preet Bharara  
U.S. Attorney, Southern District of New York

The Honorable Mary Schapiro  
Chairman, Securities and Exchange Commission

The Honorable Jeffrey Feltman  
Assistant Secretary of State for Near Eastern Affairs, Bureau of Near Eastern  
Affairs, U.S. Department of State

Riad Salamé  
Governor, Banque du Liban