

Confidential

RUSSIA

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Mikhail Mostovjuk reports from Moscow:

QUASI STATE AND ITS NON-QUASI BUDGET:

ISLAMIC STATE FINANCIAL SOURCES, RUSSIAN COUNTERMEASURES AND INITIATIVES

SUMMARY

Recently launched military operation of the Russian air force in Syria and terrorist attacks that took place in France and Tunisia as well as shooting down the Russian aircraft in the sky above Sinai, have brought new momentum to the military operation against Islamic State (IS) started by the world coalition in August 2014. Military strikes upon the territories and facilities occupied by Islamic militants are necessary to reduce the largest sources of income which those territories provide for the IS.

Constant financial support is the key factor for the terrorist network, and Russia has initiated various forms and formats of countermeasures to reduce IS financial capacity. So where does the money of the world's richest terrorist organization, whose budget can be compared to that of a small European country, come from? Mikhail Mostovjuk, Class 2 State Advisor, a long-time staff member at the Headquarters of the Ministry of Internal Affairs of Russia and a diplomatic officer, has put together opinions of experts and diplomats, as well as the Financial Action Task Force on Money Laundering (FATF) and UN Security Council reports. In the current issue of "Russia Confidential" the expert will also briefly discuss the main initiatives of Russia to block the illegal cash flow that gives terrorists regular financing.

COMING AGAINST THE REVENUE POTENTIAL OF ISLAMIC STATE: OBJECTIVES AND OBSTACLES

In light of the recent blasts of terrorist attacks in the world, responsibility for which has been assumed by the *Islamic State* terrorist organization (IS), the world community and the media follow the course of the military operation launched against the IS by the Russian aerospace forces and the Coalition led by the U.S. with particular attention. IS distinctive feature is that it declares itself as a "state" of Islam, strives to expand the territory under its control, and deals with infrastructure and administration of captured facilities and residential areas. Military strikes against territories captured by militants have well-defined goals to eliminate the terrorist network infrastructure and thus reduce its financial capacity.

- *As of today, IS is the wealthiest terrorist organization in the world. According to the data of October 2015, its annual income is around 2.5 billion US dollars, which is comparable with the budget of a small European country. To plan and to approve of its annual budget, IS employs highly qualified specialists.*
- *The number of Islamic fighters who joined the IS mercenary army is estimated at 30 thousand people, and monthly cost of up-keeping the army is 12 million US dollars. An ordinary Islamic fighter earns about 400 US dollars a month, which is much more than the Iraqi Government can offer the majority of its civil servants.*

The Financial Action Task Force on Money Laundering (FATF) has published a detailed report on the IS sources of income, having divided them into five main groups.

- ✓ **The first group** of income has to do with control over the occupied territories and is most important for ISIS. It includes a broad scope of activities.

1) Revenue from refining and sale of hydrocarbons i.e. crude oil and petroleum products as well as natural gas. This is the largest source of income for the IS.

The militants control 60% of oil production in Syria (where the bulk of the IS oil production is located) and seven large oil fields in Iraq. The heavy bitumen oil is sold at 26-35 (in some cases the price is reduced to 10) US dollars per barrel at local markets, as well as in the refineries of Turkish, Lebanese and Iraqi businessmen.

According to Turkish diplomatic sources, the amount of oil seized along the Turkish-Syrian border has quadrupled compared to 2011. In autumn 2015, the word was spread that most of the oil IS exports went through the territory of the Iraqi Kurdistan and Turkey. In the meantime, though the Coalition led by the USA had the capacity to block IS oil smuggling, it did not make any sufficient effort for that.

Despite the airstrikes of Russian air forces and the actions of the international anti-terrorist Coalition led by the U.S., both aimed at destroying the infrastructure of the IS oil production and reducing illicit exports of petroleum and petroleum products to Turkey, Jordan and the Kurdish Autonomous Region of Iraq, this remains the main source of income for the IS. It brings the Islamists more than 1 billion US dollars a year (of which about 600 million dollars comes from the sale of oil and 350 million dollars - from the sale of gas).

2) Sale of Antiques and Relics of the Past.

IS militants have occupied more than 4.5 thousand archaeological monuments, many of which are the UNESCO World Heritage Sites. The vast majority of them are located in war-torn regions, thereby contributing to their plundering on a large scale. There are two basic ways to profit from the relics of the past - to sell them directly and to levy the smugglers, trafficking antiques through the territory controlled by the militants. This activities bring the IS about 100-200 million US dollars per year.

3) *Illegitimate Taxation of Local Population.*

Terrorists get up to 400 million US dollars a year practicing various forms of extortion and looting in pretence of tax collection on the "State" security, personal vehicles, public transportation, and school studies.

4) *Control of Banks and Banking Activity on the Occupied Territories.*

All cash assets kept at the state-owned banks are fully owned by IS. Clients of private banks can withdraw cash from their accounts only if they pay a tax in favor of the Islamists in the amount of 5%. In general, this source of activity brings IS up to 1.6 billion US dollars a year.

5) *Human Trafficking.*

It is mainly the sale of girls; in some cases women trapped into slavery, can be bought out by their relatives. The demanded ransom is about 3,000 US dollars a person according to different sources.

6) *Income from the Agricultural Sector.*

IS controls more than 40% of Iraqi land allocated for cultivation of wheat. Direct capture of granaries allows militants to ensure a profitable legal sale of grain due to the inability to identify the farmers who harvested it. The contracts of purchasing crops from the agricultural companies make Islamists the major supplier of food to the controlled territory. Crop sales on the black market at a price of half the market average, brings the IS more than 200 million US dollars a year.

7) *Income from Mines and Enterprises Processing Natural Resources.*

The sales of phosphates alone allow the IS to replenish its income by at least 50 million US dollars a year, and sulfuric and phosphoric acid sales - by about 300 million US dollars.

8) *Income from Taxation of Transit Goods.*

Despite the sales turnover drop on the territories occupied by the *Islamic State*, certain types of goods still continue to be in circulation. Road tax in the amount of 200 US dollars is imposed in northern Iraq, and the customs tax of 800 US dollars is charged to trucks entering Iraq across the border with Syria and Jordan.

9) *Income from Denuding Iraqi Civil Servants of Their Salaries.*

Iraqi civil servants get their salaries only in the provinces beyond the control of the militants. However, upon returning to their home region, the servants are taxed by the *Islamic State*, up to 50% of the amount received. According to FATF, the size of salaries paid is equivalent to several billion US dollars, thus, the annual income received by IS is estimated at hundreds of millions of dollars.

- ✓ **The second group** of IS income, not associated directly with the control over the occupied territories, is kidnapping for ransom. According to FATF, the approximate annual yield of this activity ranges from 20 to 45 million US dollars.
- ✓ **The third group** of income is represented by donations to the *Islamic State* from individuals or through non-profit organizations. On the one hand, those donations are not a significant part in the structure of IS incomes (as distinct from the profits from oil sales, for example), but this type of cash flow always remains fairly stable. The list of countries whose citizens sponsor IS traditionally includes its neighbors - Saudi Arabia, Kuwait, Qatar, Libya, Turkey, and also Pakistan and Afghanistan where the group has public support.

- *According to estimates made by the Research Service of the US Congress, the IS has received about 40 million US dollars in donor support from Saudi Arabia, Qatar, Kuwait and the U.A.E. during 2013-2014. By destabilizing the situation, each of these countries fights for leadership in the region.*
- *During the G20 Summit in Antalya in November 2015, President of the Russian Federation Vladimir Putin noted that the IS receives funding from 40 countries, including members of the G20. Russian Intelligence Service alone recorded financial transactions supporting the Islamic State for the sum of 300 million rubles.*

As of today, there is a decline in the number of donations from the Persian Gulf countries, as their governments have classified the presence of a terrorist organization in the region as a threat to their territorial security.

- ✓ **The fourth group** of IS income is raising funds using Information and Communication Technologies:
- Media Center Al-Itisam Establishment for Media Production is actively spreading IS propaganda through social networks, organizes PR-campaigns using technologies of mass coverage of social networks' users, such as *Twitter Storm*.
- Widely applied are the technologies of crowd-funding (mass collecting of donations through the Internet), accompanied by full-fledged marketing campaigns.
- Some more subtle methods of fund-raising are also available, for example, online shops where one can buy goods with a high margin, converted into cryptocurrency and transferred to support the militants; various forums discussing Islam, with an access to special sections, dedicated to raising funds for IS, etc.

Due to the diversification and the lack of hallmarks of such financial transactions, their analysis is a tough challenge even for intelligence services.

- ✓ **The fifth group** is income / property of new members.

The share of this source of income is relatively small: militants replenishing the organization are valuable primarily as a human resource. According to FATF, by early 2015, at least 19 thousand fighters from more than 90 countries have left for Syria and Iraq to join the IS. Most of them contributed sums of money ranging from several hundred to several thousand US dollars.

COUNTERING THE FINANCING OF IS: RUSSIA'S ACTIONS AND INITIATIVES

Obviously, cutting down the permanent sources of IS income requires a combination of:

- coordinated military operations, including air strikes on militant captured territories and facilities;
- common efforts of international community to create the tools, which will detect and block the channels of legalization of criminally obtained funds that provide regular support to the terrorist group.

For its part, Russia continues to proactively strengthen countering the IS financing both at international venues and in bilateral format, while Russian air force strikes, along with the actions of the international anti-terrorist Coalition led by the U.S., create the background for reducing the largest source of income for terrorists - oil and oil-refining industry. As a result of those initiatives, there has been a decline in profit from the illegal export of oil and petroleum products to Turkey, Jordan and the Kurdish Autonomous Region of Iraq.

In addition, in February 2015, based on Russia's initiative, the UN SC adopted Resolution 2199, which secured a ban on all trade in oil and petroleum products from the IS and Dzhabhat al-Nusra (Syrian branch of al-Qaeda) and qualified such activities as the financial support of terrorism, thus constituting the basis for the imposition of targeted UN sanctions against those involved in this criminal activity.

However, in Russia's view, a number of states do not fulfill this resolution in an effective manner. The Russian proposals on the establishment of a monitoring mechanism for the implementation of resolution 2199 have been repeatedly blocked at the UN Security Council by Western partners. That stipulated the new Russian initiative in the form of a draft resolution circulated among the permanent members of the UN SC. It requires that member states take specific steps aimed at achieving the objectives identified in resolution 2199, and also includes the provision on coordination of efforts in capturing the perpetrators of terrorist acts with the Syrian authorities.

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Excerpts from the Membership Terms and Conditions at the Trialogue Club International

[...]

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3.1.3. Receive a copy of the Russia Confidential exclusive analytical newsletter by e-mail in chosen language (English or Russian). According to the Club Terms and Conditions, the transfer of the bulletin to third parties is not allowed.

[...]

3.2. Corporate Club members are entitled to:

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[...]

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4.1. All members of the Club must:

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6. Russia Confidential

6.1. The Russia Confidential exclusive analytical newsletter is issued by the Trialogue Ltd for the Club members' private use only.

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6.5. The newsletter is disseminated via e-mail between the Club members once a month in Russian or in English, depending on the choice of the Club member.

6.6. The Club member can also receive a paper copy of the newsletter in chosen language.



Dear members of the Trialogue Club International,

The 2015 Club season comes to an end, and we are glad to **invite you to prolong your membership for 2016 or 2016-2017**, if you have not done so yet.

In 2016, the *Trialogue* Club members will continue to receive our exclusive information on the foreign policy priorities of the Russian Federation, and on current threats and challenges to global security. **Five meetings of the Trialogue Club International** are planned for 2016 (four in Moscow and one abroad); Club members will receive 4 issues of the Security Index quarterly journal in electronic form and 2 issues in print (in 2016 only in Russian), **12 issues of the Russia Confidential exclusive analytics bulletin**, our informational and analytical newsletters.

As before, experts of the *Trialogue* Club International and of its partner organization PIR Center are open to an exchange of views on key international problems.

Fees for the *Trialogue* Club membership since 2016 are as follows:

Period	Individual membership	Corporate membership
01.01.16. – 31.12.16. (1 year)	50 000 rub.	80 000 rub.
01.01.16. – 31.12.17. (2 years)	90 000 rub.	140 000 rub.

We would like to remind you that the corporate membership is based on **"1+1" scheme** when **two representatives** of the organization participate in the work of the Club.

On all questions concerning the *Trialogue* Club International membership, please contact us by the e-mail secretary@trialogue-club.ru or by phone: +7 (985) 764-98-96

Sincerely,

**Chairman,
Trialogue Club
International**

Dmitry Polikanov