HAWALA AS AN ISLAMIC STATE CENTER OF GRAVITY

by

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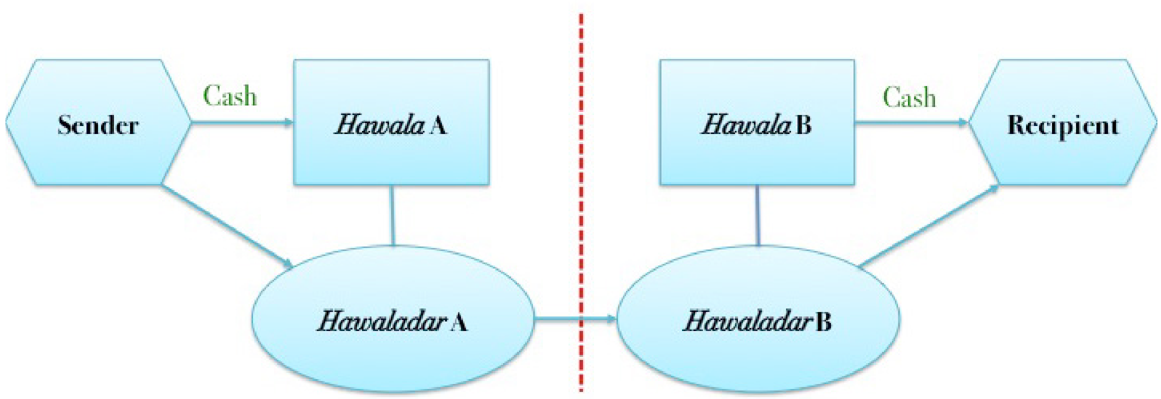
ABSTRACT

Dissecting the methods in which the Islamic State has utilized *hawalas* is an important exercise in order to better understand the group's financial, behavioral, and structural patterns. However, most reports connecting *hawala* and terror finance are often too anecdotal to systematically assess how terror groups utilize *hawalas* as part of their operations. This paper seeks to rectify this knowledge gap by analyzing the Islamic State's financial operations and organizational structure, cross referencing this information against known *hawala* operational practices to create a theoretical framework for how *hawala* factored into the Islamic State's insurgency. It concludes that *hawalas* are an Islamic State center of gravity, functioning as the foundation of the group's informal economy, and presents a plausibility argument outlining how *hawaladars* could have served critical roles as facilitators and/or leaders in the Islamic State's administrative structure.

Introduction to *Hawala*

The World Bank and the International Monetary Fund define *hawalas* as "money transfer mechanisms that exist in the absence of, or parallel to, conventional banking channels" (El Qorchi, Maimbo, and Wilson 2003, 10). The basic *hawala* transaction operates as follows. An individual in one country contacts a *hawaladar* (*hawala* operator) in his area and pays the *hawaladar* a certain amount in local currency. This payment reflects the amount the client wishes to "send" to a recipient. The first *hawaladar* then contacts a second *hawaladar* located in the area of the recipient, and this second *hawaladar* pays the recipient the amount that was "sent" in that local currency (El Qorchi, Maimbo, and Wilson, 2003, 10). Following the completion of this transaction, the *hawaladar* in the sending locale has "received funds in trust without making a payment," and the *hawaladar* in the receiving locale "has made a payment without receiving its counter value," an imbalance that must be eventually settled (El Qorchi, Maimbo, and Wilson 2003, 13).

Figure 1: Basic *Hawala* Transaction



Source: Author's drawing.

There are multiple reasons an individual would choose *hawala* over traditional banking. One prominent justification is cost-efficiency. *Hawala* transactions, even complex international ones, can be completed within one to two days, whereas formal sector transactions may require a week (Jost and Sandhu 2000). Additionally, *hawaladars* can charge low prices, such as a fee of 1-2 percent of the remitted amount, and profit from slim margins. To keep prices low, *hawaladars* can multi-purpose their existing businesses (eliminating additional overhead costs), forgo registration/reporting requirements, and engage in currency speculation. *Hawalas* are also often family operated, thereby eliminating insurance, retirement, and minimum wage considerations (Bowers 2009, 384), further lowering their cost of operation.

Hawalas also provide the user with anonymity and a low profile. The desire for anonymity could arise from the illegality of associated practices such as currency speculation, the legal status of the user, such as criminals and migrant workers, or the low literacy rate of users unable to conduct transactions through formal institutions (Bowers 2009, 385-386). Finally, *hawalas* can function in geographic areas formal institutions cannot reach or are hesitant to enter, such as “areas that are disproportionately victimized by the violence of radicals, tribal chieftains, and warlords” (Bowers 2009, 383). As such, *hawalas* tend to operate in regions where formal banking institutions are “absent or weak,” becoming more prevalent as the formal financial sector becomes more inept (El Qorchi, Maimbo, and Wilson 2003, 38).

Discussion of Previous Literature

With regard to national security, *hawalas* came to the forefront of the counter-terrorism scene following 9/11 despite the institution's limited role in the plot (Bowers 2009, 386) relative to the formal financial sector (Passas 2003, 50). Indian terror groups have used *hawalas* to finance political assassinations, and al-Qaeda (Bowers 2009, 386-387) and Hezbollah (Rudner 2010, 707) are known to have used the institution as well.

Writing on the Islamic State's predecessor, al-Qaeda in Iraq (AQI), in 2005, Looney states that while officials in Iraq were aware that Zarqawi was utilizing *hawalas*, the majority of *hawala* transactions in Iraq were legal (Looney 2005, 71). He noted that restricting access to this informal system could have upset an economy without access to formal banking measures, and that the Iraqi people would see regulation of *hawalas* as an unfair Western-demand. These concerns could explain why Iraqi politicians avoided regulation (Looney 2005, 71-72). In contrast, Williams (2005), argued that al-Qaeda made "extensive use" of *hawalas* to discreetly move money in addition to using formal sector financial mechanisms (Williams 2005). Recent reporting on the Islamic State financial structure indicates that *hawalas* are an integral, if not indispensable, component of the insurgency's effort.

In 2014, two analysts called for officials to concentrate more attention on the Islamic State's financial system, including its use of *hawalas* (Johnson and Bahney 2014a). In December 2015, the Central Bank of Iraq sanctioned around 120 exchange-houses located within Islamic State territory to prevent them from buying U.S. dollars at currency auctions (Financial Transactions and Reports Analysis Centre of Canada 2014, 2). Bauer and Levitt (2016) noted that regulatory efforts to prevent the Islamic State from receiving funds through the formal financial sector had made money-exchange "one of the Islamic State's primary means of moving money". Coker (2016) likewise addressed this development, saying that money-exchangers "ensure that millions of dollars in cash churn in and out of Islamic State's territory every day, muting international efforts to isolate the terror group from the global banking system".

A 2016 House Homeland Security Committee report stated that *hawala* played a "critical" role in Islamic State financing (House Homeland Security Committee 2016, 5), and listed *hawalas* and exchange houses as one of the means by which charity networks in the Gulf send fundraising proceeds to extremists in Syria (Homeland Security Committee 2016, 17). The U.S. Assistant Secretary for Terror Financing remarked that informal transfer mechanisms were a "portal" for the Islamic State to the outside world (Coker 2016). In December 2016, the Treasury Department sanctioned the Iraqi-based Selselat al Thahab Money Exchange, its manager, and affiliated businesses for assisting the Islamic State in purchasing weapons and ammunitions (U.S. Department of Treasury 2016).

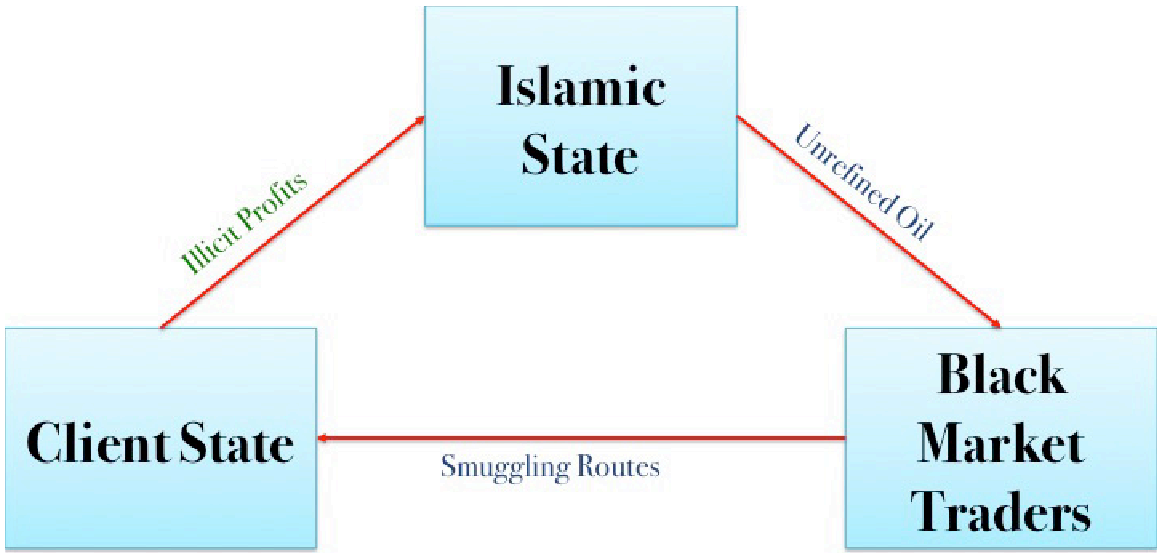
Therefore, *hawala*/money-exchanges have figured prominently into the Islamic State's financial paradigm. Dissecting the methods in which the Islamic State has utilized *hawalas* is an important exercise in order to better understand the group's financial, behavioral, and structural patterns. However, most reports connecting *hawalas* and terror finance are often too anecdotal to systematically assess how terror groups utilize *hawalas* as part of their operations. This paper seeks to rectify this knowledge gap by analyzing the Islamic State's financial operations and organizational structure, cross referencing this information against known *hawala* operational practices to create a theoretical framework for how *hawala* factored into the Islamic State's insurgency.

Hawala as an Instrument of Insurgent Economy

The Islamic State has historically avoided formal financial institutions (Johnson and Bahney 2014b). This preference is both pragmatic and intentional. Avoiding the formal financial system mitigates the effects of sanctions and other traditional tactics to limit terror-finance (Paul 2014-2015, 71-72), while the group's aspirations to become a self-sustaining pseudo-state requires "coercion and co-option" (Johnson and Bahney 2014b). As of 2014, the Islamic State's financial portfolio was composed mainly of criminal activities, including extortion, robbery, kidnapping, trafficking, and smuggling. The insurgents coopted existing criminal networks and worked with local smugglers to move weapons, oil, and people across borders (Paul 2014-2015, 71-73), something facilitated by Iraq's "porous borders," well-developed smuggling networks (Williams 2015, 164), and the longstanding tradition of smuggling in Iraq's regional economy (Williams 2015, 32).

The Islamic State's oil smuggling scheme is a critical funding source for the insurgency (Di Giovanni, Goodman, and Sharkov 2014). The smuggling process begins by selling unrefined oil to black market traders who then utilize smuggling routes through occupied territory to carry the product to its terminal destination. Several hotspots for the Islamic State's vast financial/oil network include Turkey's southern corridor, Iraq's northwestern corridor, Syria's northeastern corridor, and Iraqi Kurdistan (Di Giovanni, Goodman, and Sharkov 2014). Johnston and Bahney posited that the Islamic State prefers to repatriate oil profits "either through money laundering or through informal financial institutions" (Johnson and Bahney 2014a). Likewise, researchers at the RAND Corporation note that "Moving resources, such as oil, refined oil products, phosphates, and even antiquities, requires intermediaries and transport," and argue that formal financial institutions would be unlikely to serve this purpose (Johnston *et. al* 2016, 272-273).

Figure 2: Islamic State Illicit Oil Smuggling Scheme

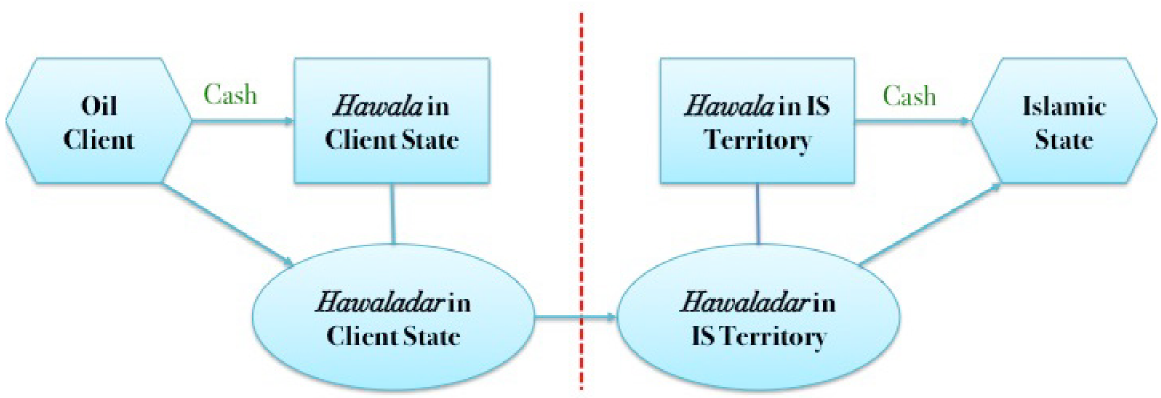


Source: Author's drawing.

Hawalas and exchange houses are prime candidates for repatriating the Islamic State's illicit profits. However, evidence for this process is difficult to find and verify. Although one of the exchange houses sanctioned by the Central Bank of Iraq processed transfers to Mosul totaling $50,000 from Iraqi and Syrian clients in Istanbul, the workers did not ask for details regarding the transaction (Coker 2016). Thus, the affiliation of the individuals, purpose of the transaction, intended recipients, and the composition of the $50,000 as either a lump sum or summation of multiple clients is unknown. However, because the Turkish border is a preferred avenue for transfers into Iraq and Syria given the lower levels of security (Di Giovanni, Goodman, and Sharkov 2014), this report demonstrates the ability of *hawalas* and exchange houses to transfer large volumes of money from known oil client regions into Islamic State territory. Thus, I outline a hypothetical framework for how these informal financial systems might repatriate profits.

Once the crude oil reaches it terminal location, the client would deposit payment as cash at a local *hawala*. Assuming this transaction is purely bilateral, this *hawaladar* would contact another *hawaladar* within his network located in Islamic State territory. The *hawaladar* located in Islamic State territory would then pay out the profits as cash to an Islamic State financial agent. In this exchange, the *hawaladar* in the client state has incurred a liability, while the *hawaladar* in Islamic State territory has gained an asset. There are a host of methods these *hawaladars* could utilize to balance accounts.

Figure 3: Oil Profit Repatriation



Source: Author's drawing.

One option is a basic reverse *hawala* transaction. In this case, accounts are rebalanced as individuals within Islamic State territory deposit money in the *hawala* that paid out the profits earlier (replenishing that *hawaladar*'s cash pool) to remit to individuals located in the client state. The *hawaladar* in the client state then draws from his cash pool to handle these remittances, thus balancing accounts. Though simple, reverse *hawala* is unlikely and suffers from several shortcomings, as it requires that money goes through the same two *hawalas*, and that the aggregate value of the goods purchased and money remitted *into* Islamic State territory equals the value of goods sold and money remitted *out of* Islamic State territory (El Qorchi, Maimbo, and Wilson 2003, 23-24). Another option is cash couriers, but this process suffers from logistical burdens.

> The principal drawback of using couriers is one of logistics. One million dollars in "street cash" (i.e. bills in \$5, \$10, and \$20 denominations) weighs approximately 256 pounds. Therefore, in larger transactions, some hawaladars (or their associates) utilize import/export businesses. (Bowers 2009, 380-381)

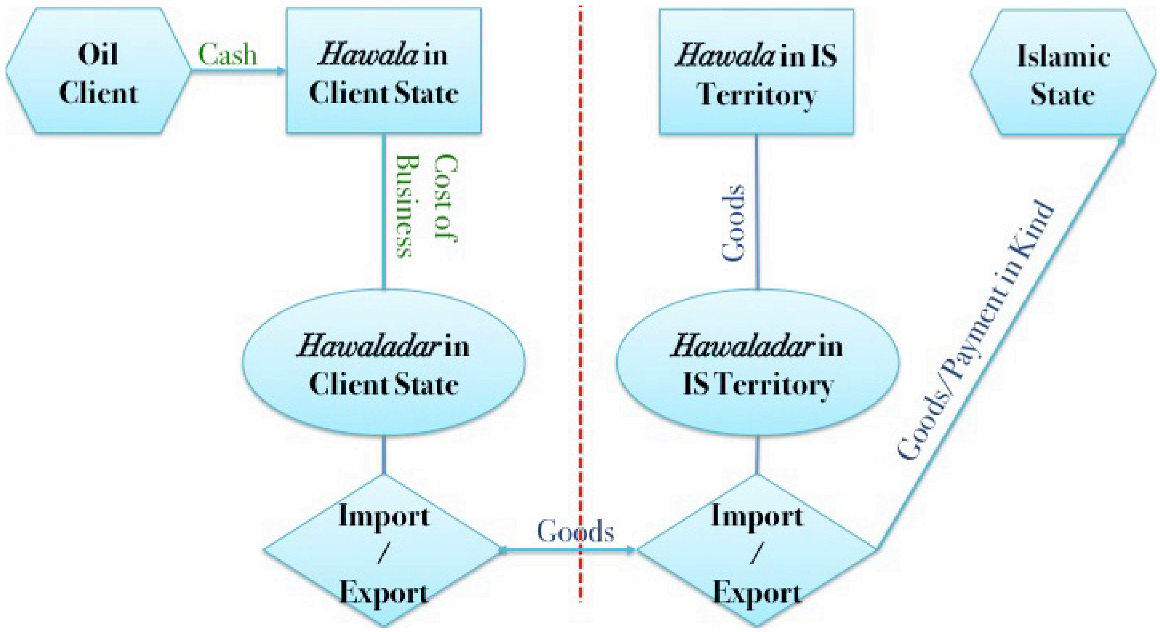
Balancing accounts through trade can occur bilaterally through respective side businesses (import/export) owned by the *hawaladars*, or by transferring claims and obligations to a third party (El Qorchi, Maimbo, and Wilson 2003, 24-25). Since *hawaladars* are known to reutilize business infrastructure to reduce overhead costs, such an arrangement is plausible

> Money flows easier than water," said an Iraqi trader named Kemal who uses another Turkish-Iraqi company, Taha Cargo, to transfer funds out of Islamic State, and then employs its logistic network to ship goods in return. Taha didn't respond to requests for comment. (Coker 2016)

A hypothetical trade within the oil smuggling framework could proceed as follows. Once the crude oil has reached the client state, the recipient would deposit payment as cash to a local *hawaladar* who absorbs this payment as a cost of doing business. That *hawaladar* repurposes these funds to purchase goods that are then shipped through his import/export business to another *hawaladar*'s import/export business in Islamic State territory. The

Islamic State could coopt this import/export capacity to receive payment in kind (necessary supplies/materials) for its oil exports.

Figure 4: Repatriating Profits Through Bilateral Trade



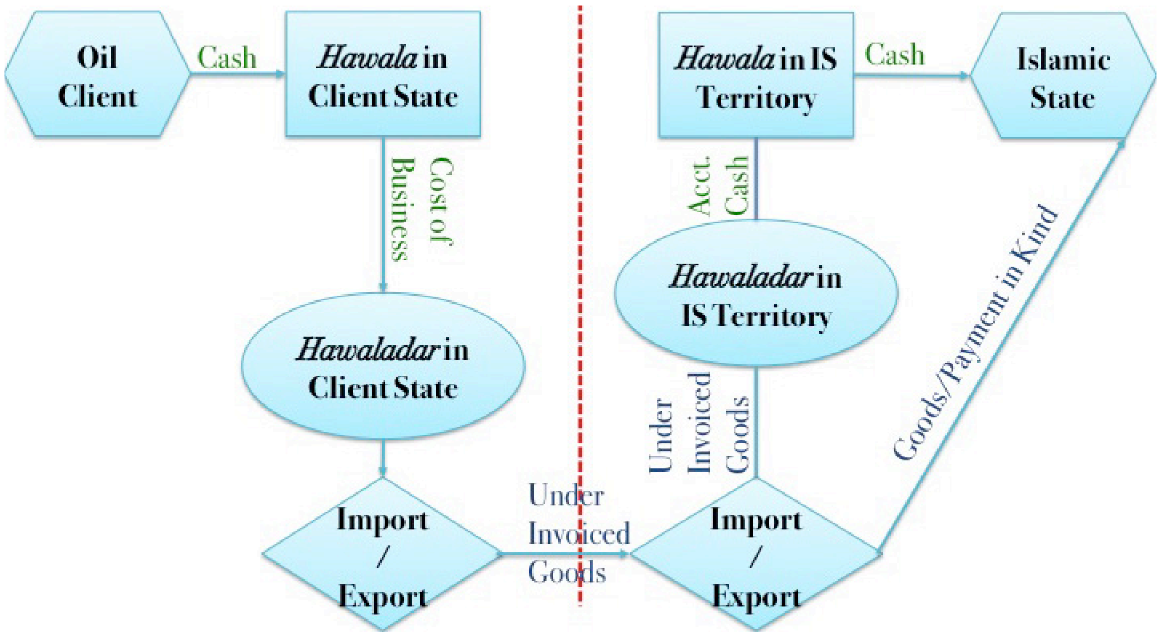
Source: Author's drawing.

A variation of the trading arrangement is over/under invoicing product shipments (El Qorchi, Maimbo, and Wilson 2003, 25).

> Through over-invoicing of exports one effectively receives money. For example, if I ship goods worth US$100,000 to Bangladesh but invoice my business partner for $150,000, I will be receiving an additional $50,000 in the US. (Passas 2003, 52)

In the illicit oil trade, the *hawaladar* in the client state could *under-invoice* exports to the *hawaladar* in Islamic State territory, shipping goods with a greater actual value than shown on paper. This generates de facto money for the *hawaladar* in Islamic State territory, settling liabilities through accounting manipulation. If the Islamic Sate coopted this process to repatriate its oil profits, the *hawaladar* in the client state would have to under-invoice his exports into insurgent territory by the same dollar amount of the oil sale (plus any additional amount needed to settle accounts with his counterpart *hawaladar*).

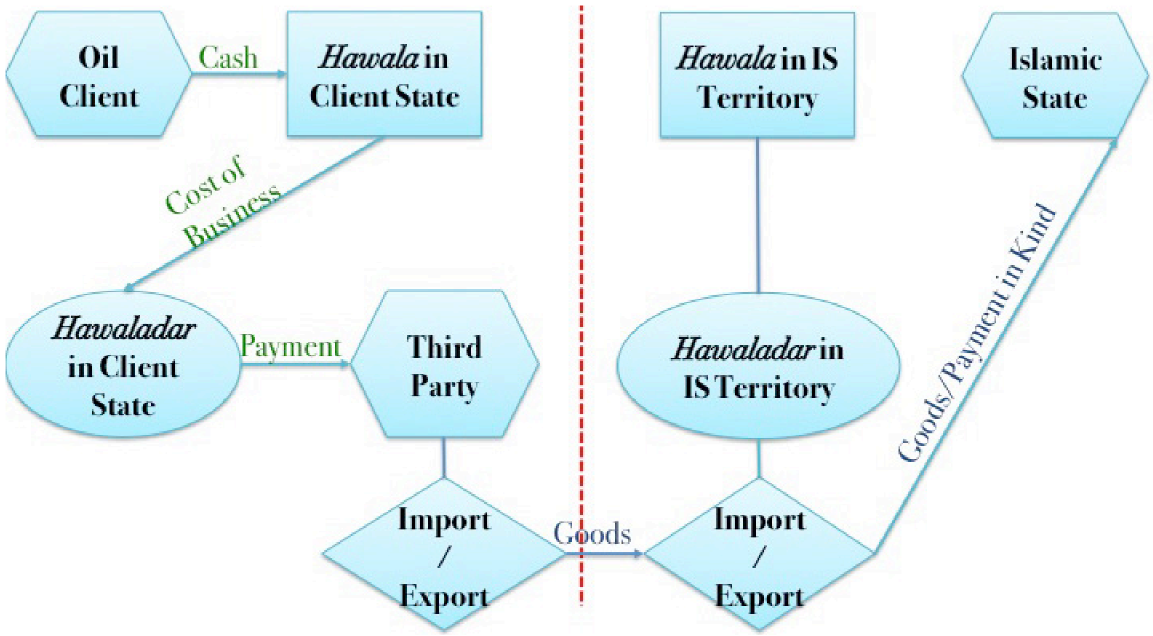
Figure 5: Repatriating Profits Through Bilateral Trade/Invoice Manipulation



Source: Author's drawing.

Trading arrangements to balance accounts suffer from the same shortcomings as reverse *hawala* and require a double-coincidence of wants. The *hawaladar* in the client state must operate an import/export business capable of supplying the specific goods requested by the *hawaladar* in insurgent territory and by the Islamic State. Otherwise, using bilateral trade to settle accounts and/or repatriate oil profits through payment in kind would be impossible. A multilateral trading network mitigates this problem. Here, the *hawaladar* owing the liability finances the exports while a third party handles the actual shipping of goods (El Qorchi, Maimbo, and Wilson 2003, 25). Thus, after the oil client has submitted payment to a *hawaladar* in the client state, this *hawaladar* repurposes these funds to purchase goods in a third country. Another economic agent (perhaps another *hawala* or independent import/export business) ships these goods to the *hawaladar* in insurgent territory.

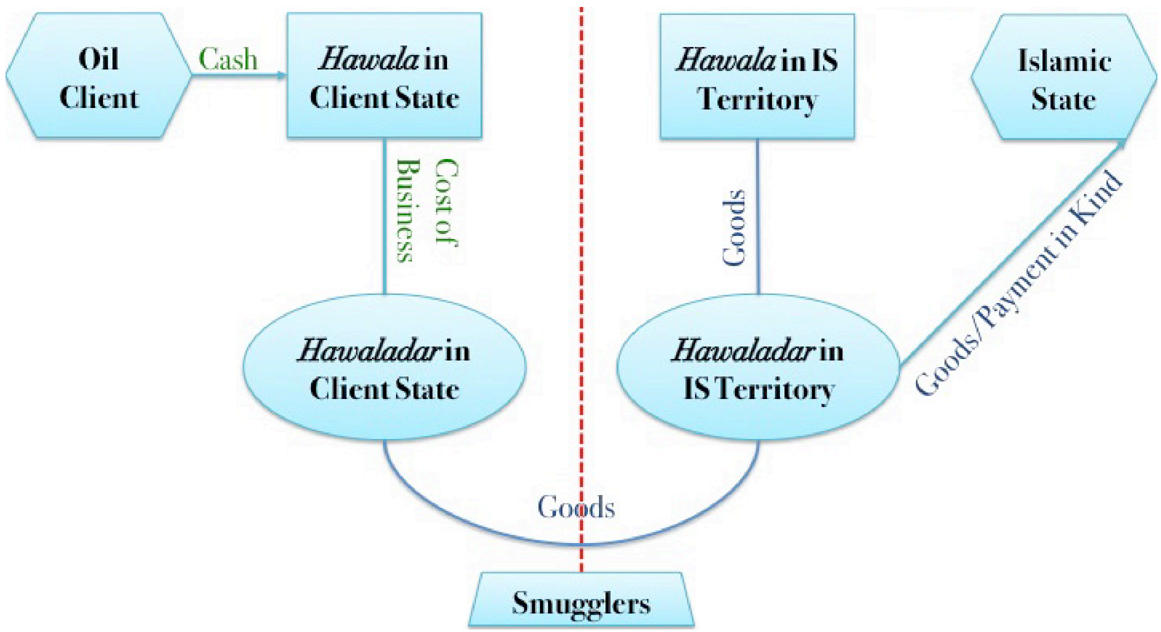
Figure 6: Repatriating Profits Through Multilateral Trade



Source: Author's drawing.

Accounts settled via smuggling follow the same trading procedures discussed above, but "without the complication of declaring the trade flow or associated payments" (El Qorchi, Maimbo, and Wilson 2003, 25).

Figure 7: Repatriating Profits Through Smuggling



Source: Author's drawing.

Hawaladars may operate their own independent smuggling ring, or cooperate with regional smugglers as part of a larger black market financial/commodity-trading network. There are four warrants for this latter possibility.

1. One of the unique hallmarks of *hawalas* is the prominent role of personal networks (El Qorchi, Maimbo, and Wilson 2003, 10). Most scholars seem in agreement that the composition of a *hawala* network is often familial, ethnic, or religious. Indeed, a *hawaladar* often shares his clientele's ethnicity (Soudjin 2015, 263-265), something amplified "in rural areas where rarer dialects, lesser-known traditions, and a general distrust of outsiders act as further barriers to entry" (Bowers 2009). *Hawala* users interact informally outside of transactions, and *hawaladars* are prominent, sustained fixtures in their locales and maintain extensive ties over time (Razavy and Haggerty 2003, 147). Such high connectivity and well-developed personal networks would make *hawaladars*

attractive to smugglers, who must operate under the radar and avoid interdiction by law enforcement authorities.

2. *Hawalas* have proven capable of managing competing factions to facilitate business continuity. At least three money-exchangers with alleged ties to the Islamic State employed Shiite and Kurdish militias to protect cash shipments to Islamic State territories. Though both these militias fight against the Islamic State (Coker 2016), they escort exchange-house cash shipments destined for regions occupied by their opponent. If *hawaladars* serve as intermediaries between combatants, they could certainly serve as intermediaries between border/law enforcement and smugglers to safeguard smuggling operations.

3. *Hawaladars* could preserve a smuggler's need for anonymity and discretion. The informality of *hawala,* and the lack of formal adjudicating agents, is counteracted by a "cultural valorization of personal reputation and family honour" (Razavy and Haggerty 2009, 147-148). Unpaid debts carry repercussions for the *hawaladar*'s family and tribe (Coker 2016). In one study on the criminal use of *hawalas*, *hawaladars* did not ask questions even if they had reasons to be suspicious (Soudjin 2015, 270). This low profile, high degree of integrity, and commitment to secrecy would benefit local smugglers evading authorities.

4. *Hawalas* could make cash-heavy, cross-border black market exchanges more manageable. One study on *hawala* use in money laundering observed that criminal actors use *hawalas* to exchange smaller denominations for larger denominations to make money transit easier (Soudjin 2015, 267-268). Exchange houses in Iraq participated in bi-monthly dollar auctions, ordering over $20 million in $100 bills (Coker 2016), before the

Central Bank of Iraq excluded houses located in or around Islamic State territory (Financial Transactions and Reports Analysis Center of Canada 2016, 2). Such access to higher denominated bills could aid interested smugglers with bulk cash shipments.

Thus, when the Islamic State coopted regional smugglers, it might have also incidentally (or intentionally) incorporated *hawalas*. This three-pronged partnership would have amplified the insurgency's geographic reach, and could explain the sophisticated logistics mechanisms observed in the Islamic State's supply chain. A 2014 report from Conflict Armament Research (CAR) noted that the Islamic State's rapid weapons movement from Mosul, Iraqi to Ayn Al-Arab Syria (a distance about 500 km) during a two-week period "demonstrates the logistical competence of IS forces" (Conflict Armament Research 2014, 6). A later report from CAR stated that "IS forces have manufactured and deployed improvised explosive devices (IEDs) across the battlefield on a quasi-industrial scale," and noted that IED "chains of supply differ from those of military weapons" (Conflict Armament Research, 2016, 6).

> In all identified cases, producers have lawfully traded components with regional trade and distribution companies. These companies, in turn, have sold them to smaller commercial entities. By allowing individuals and groups affiliated with IS forces to acquire components used in IEDs, these small entities appear to be the weakest link in the chain of custody. (Conflict Armament Research, 2016, 7)

The report goes on to say that "many small-scale commercial enterprises appear to have sold, whether wittingly or unwittingly, components to parties linked to, or employed by, IS forces" (Conflict Armament Research, 2016, 7). Movement of these components from commercial entities to the Islamic State occurred rapidly (Conflict Armament Research, 2016, 7). Turkey was particularly important in the Islamic State's IED supply chain, and CAR mentions the possibility that Islamic Sate intermediaries "acquired the components in Turkey and subsequently transferred them to Iraq and Syria" (Conflict Armament Research, 2016, 11).

Such speed of weapons transit could suggest a high freedom of movement, or a strategic partnership with local financial intermediaries and logistics networks. As noted earlier, the owner of the Iraqi-based Selselat al Thahab Money Exchange maintained a branch in Albu Kamal, Syria that the Islamic State used for weapons and ammunitions deals (U.S. Department of the Treasury 2016). This exchange house could have been just one of many similar intermediaries servicing the Islamic State's weapon's supply chain. Thus, in addition to illicit oil profit repatriation, *hawalas* may facilitate weapons and other critical supplies transfers. If the Islamic State coopts a *hawala*, the *hawaladar* might add layers of protection and ambiguity to evade detection. For example, a *hawaladar* in an oil client state could utilize a cash courier to repatriate a portion of oil profits. He could then purchase goods as payment-in-kind shipped into insurgent territory through his import/export business, a third party, or a combination of both. These shipments may be under/over invoiced, further disguising the nature of the transactions. Further, "Mid- level hawaladars act as clearing houses for small scale operators, larger hawaladars act as clearing houses for those in the middle, and so on" (Bowers 2009, 380). Thus, the process could become very convoluted.

Hawalas also play a key role in cementing the group's position and staying power in the region's informal economy. Looney writes that Iraq's informal economy has been a significant force in the country since April 2003, estimating in 2006 that it comprised at least 65 percent of GDP and employed 80 percent of the labor force (Looney 2006, 1006). The significance of the informal economy increases as uncertainty in government policy and credibility rises (Looney 2006, 994). As a result of living in a volatile locale, many Iraqi's have adopted a cautious mindset with regard to economic development and enterprise.

> In an environment of several decades of political and economic insecurity, doubt and distrust are deeply entrenched in the individual mind. They represent a major constraint against drawing entrepreneurs and individuals out of the safe, kinship-based informal economy. (Looney 2006, 999-1000)

The Islamic State's control of cross-border territories and integration into criminal and smuggling networks builds its revenue sources, market for goods/services, and partners and clients. Integration into the illicit economy by establishing mutually beneficial arrangements could lengthen conflict with the group (Paul 2014-2015, 76). Thus, the Islamic State's integration with *hawalas* and exchange houses can consolidate the group's regional influence over local centers of power. These informal financial institutions "move the wheels of Iraq's economy" as one of the limited means to procure food and clothing (Yahya al-Kubaisi quoted in Coker 2016). In order to project longevity and influence, the Islamic State needs to bolster the strength and attractiveness of the informal sector and manufacture uncertainty and distrust to drive people away from the formal sector. This happens in several ways.

1. The Iraqi government must compete with informal financial institutions, and more generally, the informal economy, for tax revenue (El Qorchi, Maimbo, and Wilson 2003, 30-31). Since the Islamic State exerted control in Iraqi territory, the informal

financial sector experienced an uptick in business profitability. The insurgent invasion of Mosul in June 2014 effectively shut down the local banks, due to both the ensuing looting and the international response to sanction compromised financial institutions. As a result, *hawalas* and money exchangers became the "sole providers for a region covering several million people" (Coker 2016). The rates charged for financial transactions through Islamic State territory were sometimes seven percentage points higher than before. The Islamic State was quick to capitalize on the profitability, requiring a 10% *zakhat* tax for transfers out of its territory and levying a 2% tax on cash shipments entering the territory bound for exchange houses (Coke 2016). This represents not only a source of direct funding for Islamic State activities, but also a significant revenue loss to the Iraqi government.

2. As mentioned before, Iraqi exchange houses in Islamic State territory participated in bi-monthly dollar auctions, ordering over $20 million in U.S. currency. The difference between the official exchange rate and the parallel or black market rate would have allowed these exchange houses to generate a $330,000 profit in money sales, providing a substantial revenue source for Islamic State taxes (Coker 2016). Moreover, whenever the difference in the black market and official exchange rate widens, the informal financial sector grows in significance. This expansion has the effect of increasing the exchange rate differential, perpetuating the cycle (El Qorchi, Maimbo, and Wilson 2003, 29). Therefore, the longer black market exchange operations offer a competitive alternative to the formal sector, the more the Islamic Sate gains through taxes on *hawala* and exchange houses.

3. The Islamic State may benefit from the very policies designed to curtail its access to foreign currency. In 2015, the Federal Reserve ceased providing cash shipments to Iraq for fear that Islamic State militants were profiting from dollar auctions. As a result, Iraq was sent into a cash crisis (later relieved after officials provided more transparency) (Coker 2016). Prior to this ban, "Iraqi dollar procurements had tripled between 2012 and 2014" (Bauer and Levitt 2016), indicating that demand for foreign currency was high. *Hawaladars*, through logistics, import/export, and smuggling connections, would have been well positioned to meet this demand for dollars during the shortage. If the formal sector was significantly strapped for dollars, banks might have been forced to procure foreign currency from *hawalas* and exchange houses, legitimizing the Islamic State's financial brokers.

> In some countries (such as Pakistan), the shortage of foreign exchange in the official market has required central banks to purchase foreign exchange from the black markets. Such a move indirectly influences the level and composition of broad money. Purchases from the parallel market entail a "recycling" of foreign currency into the formal sector through increases in central bank foreign assets, but foreign currency would be supplied by foreign correspondents of money changers or other intermediaries (El Qorchi, Maimbo, and Wilson 2003, 30).

While the freeze on cash shipments was eventually lifted, a more sustained dollar deficit may allow insurgent groups like the Islamic State to isolate the formal sector from currency acquisitions, sustaining the economic uncertainty, distrust, and chaos. Such economic warfare depends on the Islamic State's ability and willingness to pressure *hawala/*exchange-house operators to not sell foreign currencies to formal sector clients.

The Islamic State has demonstrated that it will exercise harsh and brutal tactics to control a local population (Khatib 2015, 9), so intimidating *hawaladars* to comply with demands is not beyond question. This presents an important consideration for U.S. policymakers seeking to isolate the Islamic State from the financial market. Sanctions on the formal sector could have the unintended effect of strengthening the group's position in the informal economy, while weakening and degrading the influence of formal institutions and authority. Since economic uncertainty works to the Islamic State's benefit, driving more individuals to the informal institutions under its influence cements the group's staying power.

Hawala as an Instrument of Insurgent Administration

In 2014, then Treasury Undersecretary for Terrorism and Financial Intelligence, David Cohen, stated that the Islamic State "depends on complex management networks with [chief financial officer]-like figures at the top" (quoted in Di Giovanni, Goodman, and Sharkov 2014). The next section of this paper presents a plausibility argument that *hawaladars*/exchange-house operators may fulfill these financial managerial roles. In order to accomplish this, this section draws heavily on two studies from the RAND Corporation to approximate the Islamic State's current organizational typology and financial flow patterns. The first analyzed al-Qaeda in Iraq (AQI) primary source records from Anbar (2005-2006) (Bahney *et. al.* 2010, 2), and the second extended on this research by examining Islamic State in Iraq (ISI) records from Baghdad (2007), Ninewa (2008-2009), and al-Jazirah (2010) (Johnston *et. al* 2016, 185). RAND reports that as recently at 2016, the Islamic State still used certain AQI and ISI internal structures, including "organizational culture, personnel policies, and administrative policies"

(Johnston *et. al* 2016, xv-xvi). Additionally, ISI's organizational system in 2008 matches reports on the Islamic State's organizational system in 2015, with "managerial responsibilities and structures" mainly unaltered (Johnston *et. al* 2016, 253-254). Thus, RAND's finding on AQI and ISI's structure provides a good proxy for the Islamic State's structure.

RAND's study on AQI's organization highlights two roles that figure prominently into future discussion: a provincial general emir, and a provincial administrative emir. Individuals in these positions "served as key decision makers for the allocation of finances between the sectors, directing funds to and collecting revenues from each" (Bahney *et. al.* 2010, 31). Direct evidence regarding the existence of these positions in the Islamic State's most recent network was not uncovered in the scope of this research. However, given the repetitious nature of the group's organization, its reasonable to expect that the Islamic State retained these positions or some variation of this position.

The general emir rarely oversaw the allocation of funds to sector or subsidiary offices, leaving this task to the administrative emir (Bahney *et. al.* 2010, 44). The administrative emir held little cash on hand (Johnston *et. al* 2016, xiv), but moved large amounts the same day it was received. This was distributed to provincial administrative units, local military wings, or the General Treasury (Johnston *et. al* 2016, 43-44).

> The administrator of Anbar balanced his books and updated his master accounting sheet biweekly. As noted above, the administrator saved very little revenue. We believe that this behavior was intended to provide a high level of operational tempo across the province in the short run, because it was a known goal of AQI to

> sustain high attack levels to sap the Coalition's willingness to remain in Iraq. (Johnston *et. al* 2016, 43-44)

Sometimes funds from sector units were sent directly to the administrative emir (rather than the sector emir). RAND provided two explanations: either the administrative emir held businesses assets in those sectors, or this was a procedural requirement based on seniority. While RAND argued for the latter (Johnston *et. al* 2016, 193), there are six reasons to suggest why the administrative emir could have operated a *hawala/*exchange-house business on the side.

1. The pattern of moving large quantities of cash in quick succession is reminiscent of *hawaladar* behavior in Islamic State territory. For example, one currency exchange operator in Anbar transferred $500,000 weekly through Islamic State territory (Coker 2016). If the administrative emir operated an informal financial institution, he could use his *hawala* to perform administrative duties on behalf of the insurgency, taking a portion of each transaction as personal profit. Such an arrangement would not only be beneficial financially, but also expedite operations since he would be working through a network that is already known and trusted. Further, since non-fighting positions in the Islamic State's administration earn $200 monthly (Kamal and Ouad 2015), the profitability of such a dual role may lead some *hawaladars* to submit to Islamic State authority (either willingly or under duress).

2. *Hawaladar*'s serving dual roles as administrative emirs would increase the insurgency's legitimacy. The Islamic State has a demonstrated tendency to incorporate local tribal actors into its administrative infrastructure. Drawing clan members into the fold and leveraging their influence to garner wider support projects the appearance of

strong tribal alliances with the insurgency (Kamal and Ouad 2015). Because the composition of a *hawala* network is often familial, ethnic, or religious, and because *hawaladars* are prominent fixtures in communities wary of outsiders, coopting *hawaladars* to fulfill administrative roles could provide the Islamic State similar sociopolitical capital in its area of operation.

3. Beyond building the group's sociopolitical capital amongst indigenous populations, local figureheads serving in managerial positions might also aid recordkeeping integrity. Administrative emirs assigned members a personally identifying serial number and collated information on member demographics, skills, operational roles, unit assignments, number of dependents, and "killed or captured" status (Johnston *et. al* 2016, 106, 156, 170). This recordkeeping provided leadership a report on unit attrition levels, a function both unique to the administrative emirs and critically important for efficient human and financial resource allocation (Johnston *et. al* 2016, 170). A *hawaladar's* longstanding ties to the community and local knowledge amassed as a result could help ensure the accuracy of these reports.

4. *Hawaladar*'s could help supply and manage the Islamic State's ancillary militant network, which comprises the group's "core defensive manpower" (Knights 2014, 5-6). The Islamic State has received pledges of allegiance from thirty-four radical Islamist groups and has fighters from 120 nations (House Homeland Security Committee 2016, 3). Smuggling networks have been critical in transporting recruits into Iraq (Williams 2015, 232). If *hawaladars* were in fact highly integrated with smuggling networks as this paper posits, their assistance in transporting recruits across borders

would be invaluable. Serving as an administrative emir, they would immediately be able to record country of origins, special skills, and any other data of interest on the recruits.

5. *Hawaladar*'s could help ensure internal security and prevent breaches by coalition or security forces. While military alliances and a large foreign fighter network carry benefits, it also creates certain vulnerabilities. ISI was "heterogeneous" relative to other insurgency groups because of its diverse foreign fighter network, and could not rely on "preestablished social networks to ensure the trustworthiness of personnel and communicate a shared understanding of current conditions" (Johnston *et. al* 2016, 51). The Islamic State suffered from a similar vulnerability, but adjusted in a variety of ways. Because coalition airstrikes require intelligence on Islamic State leadership, new foreign fighters are viewed with caution. Given the high financial burden of vetting these potential spies, leaders are exercising extreme caution by not disclosing addresses and ordering suspicious characters killed (Khatib 2015, 23). A central authority tightly regulates Twitter accounts, and commanders are not photographed and their faces are not publicized until after their deaths (Khatib 2015, 13).

> ...former ISF must register themselves and repent, commencing an evaluation process whereby such individuals may be recruited, taken as hostages or killed. ISIL usually already has some background in the area after years of studying and interacting with local communities, so its regime security measures are often well-informed. (Knights 2014, 5)

The Islamic Sate's local connections shielded the group from informants, protecting against information breaches. Administrative emirs, as "the only element in the ISI organization with full knowledge of the status of all units operating in their areas of responsibility" (Johnston *et. al* 2016, 170), and as the agents responsible for overseeing funding to ancillary military groups (via the provincial administration) (Bahney *et. al* 2010, 32), would be highly involved in the process of procuring, vetting, managing, and funding the Islamic State's militant network. A *hawaladar* that employs local militias to protect cash shipments, such as the one discussed earlier, would have the requisite knowledge of regional militant groups to ensure that new alliances and recruits are benign to the Islamic State.

6. The efficiency of *hawalas* could allow the Islamic State to maintain its operational tempo even during periods of high kinetic activity from coalition and security forces. The AQI provincial administration redistributed funds from higher earning to lower earning sectors or strategically important units (Bahney *et. al* 2010, 41, 74). *Hawalas* are highly cost effective, capable of completing complex international transactions in one to two days and functioning in tough geographic areas marked by violence. *Hawaladars* serving as administrative emirs could leverage logistics/courier networks and regional counterparts to conduct secure transnational/trans-regional cash movement. This ability is useful during austere battle conditions, as seen when ISI moved funds to regions with little support or when it was under attack by Sunni Awakening and Iraqi forces (Johnston *et. al* 2016, 228).

It is not necessary that a *hawaladar* adopt the Islamic State's extremism to serve in a managerial capacity. The decision to work as an administrative emir could be entirely pragmatic, driven by a profit motive, or survivalist. Further, rather than serving as administrative emirs directly, *hawaladars* could function as facilitators to administrative emirs by performing the logistical heavy lifting and providing local information and expertise. Assuming multiple roles and allegiances amidst the many players in Iraq's complex conflict is not uncommon.

> There is a misperception among analysts and those unfamiliar with Iraq and al Anbar that insurgents, militias, death squads, security forces, and local al Qaeda members are all entirely separate entities. In truth, many in Iraq pledge allegiance to more than one cause, meaning various groups could count on many of the same individuals within the general populace to support their causes, from providing personnel to logistics support to navigating unknown territory. (McAry 2009, 52)

Thus, *hawaladars* may simply be intermediaries, servicing the various groups (criminal elements, smugglers, Islamic extremists, average citizens, other *hawaladars*, etc.) with stakes in the Iraqi conflict but remaining an impartial actor. Nevertheless, the possibility of radicalization should not be discounted either, as one author noted that "bandwagon" approaches can morph to actual radicalization the longer ties with the Islamic State are maintained (Knights 2014, 5-6). The final section places *hawala* and administrative emirs in the context of theoretical discussions on terror network disruption.

Hawala as an Instrument of Insurgent Network Disruption

Network analysis of criminal structures allows law enforcement officials to neutralize critical junctures in a network's apparatus, such as "information holdings and communication patterns," and reveal "which individuals and relationships are most vulnerable, and most important to the operations of the network." Network analysts consistently point to identifying the central-most actor as the prime target for network disruption (Strang 2014, 18). One approach for finding this central-most actor is through financial analysis, as "following money flows can assist in mapping the network and identifying previously obscured or unknown nodes and connections" (Williams 2005). Commodity flow and financial flow analysis of criminal markets can provide insight into the critical junctures that would hamper market function, such as supply chain and money laundering operations/operatives. This approach can apply to terrorist groups that integrate with criminal markets (Strang 2014, 16-17). Since the Islamic State's financial portfolio was mainly composed of criminal activities and it coopted criminal and smuggling networks, financial flow analysis is useful in unlocking the groups central-most actors.

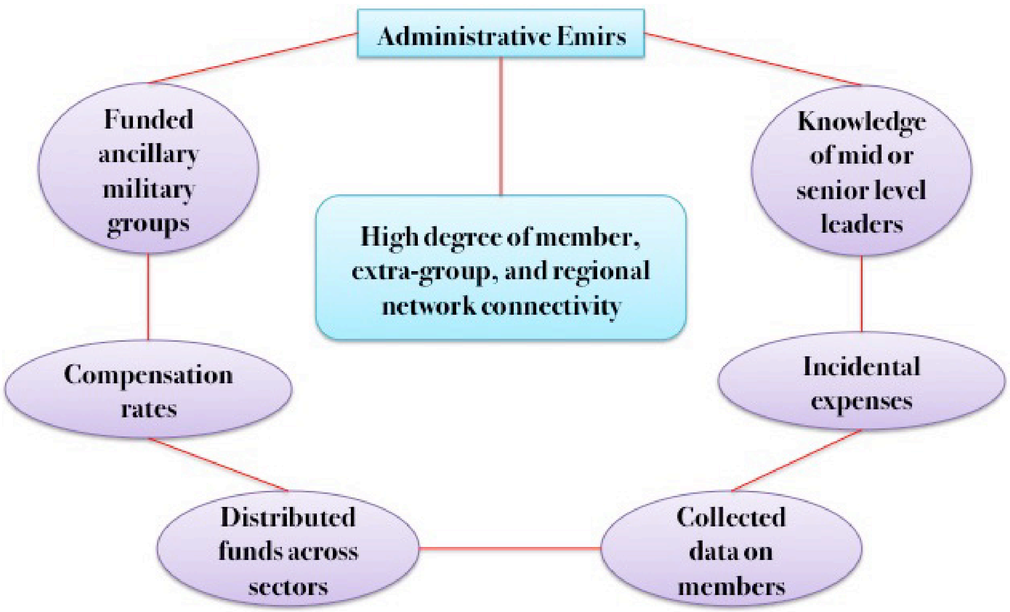
In a decentralized network, the leader plays the role of a guide, motivator, and goal setter, while the financial manager performs the actual leadership responsibilities. The finance manager directs all other managerial roles (propaganda, security, equipment); provides direct instruction to militants; has the most contact with other members; maintains the sole direct link to the group leader; funds cells and operatives in various geographic locations; commands the most regional relations; supplies member salaries and additional funds for operations; and has extra-group ties to organizations and acts as a "gatekeeper" (Berzinji 2011, 23). Thus: "Since the finance manager has most of the operational capacity in a terrorist network tracking his activities or apprehending him will cause the most harm to the operational capabilities of the group" (Berzinji 2011, 21).

With regard to the Iraqi insurgency, AQI was organized and bureaucratic as early as 2005 (Johnston 2016, 4), but practiced "decentralized decision making" (Bahney *et. al* 2010, xvi). Similarly, ISI utilized Iraqi natives for "handling street-level financial activities" (Johnston 2016, 266). The Islamic State maintained the organizational hierarchy and decentralized decision-making of both its predecessors. Knights assessed that Abu Bakr al-Baghdadi's command and control structure was one of "centralized control but decentralized execution," where attack dates were established by the command cell but executed at the provincial level (Knights 2014, 3). Bilger stresses that the Islamic State allows some local operational freedom but still executes "nation-wide changes to its tactics," demonstrating "a unified, coherent leadership structure that commands from the top down"(Bilger 2014, 9). Similarly, in a personal email correspondence on April 15, 2017, Samuel Simon Jr. (a counterterrorism authority), argues that the Islamic State

> ...has evolved from the traditional terrorist organizations of the 1980-2000 era. They are far more decentralized in their membership and leadership. However they control a formidable armed force that has allowed them to occupy and rule over vasts [sic] tracts of land in both Syria and Iraq.

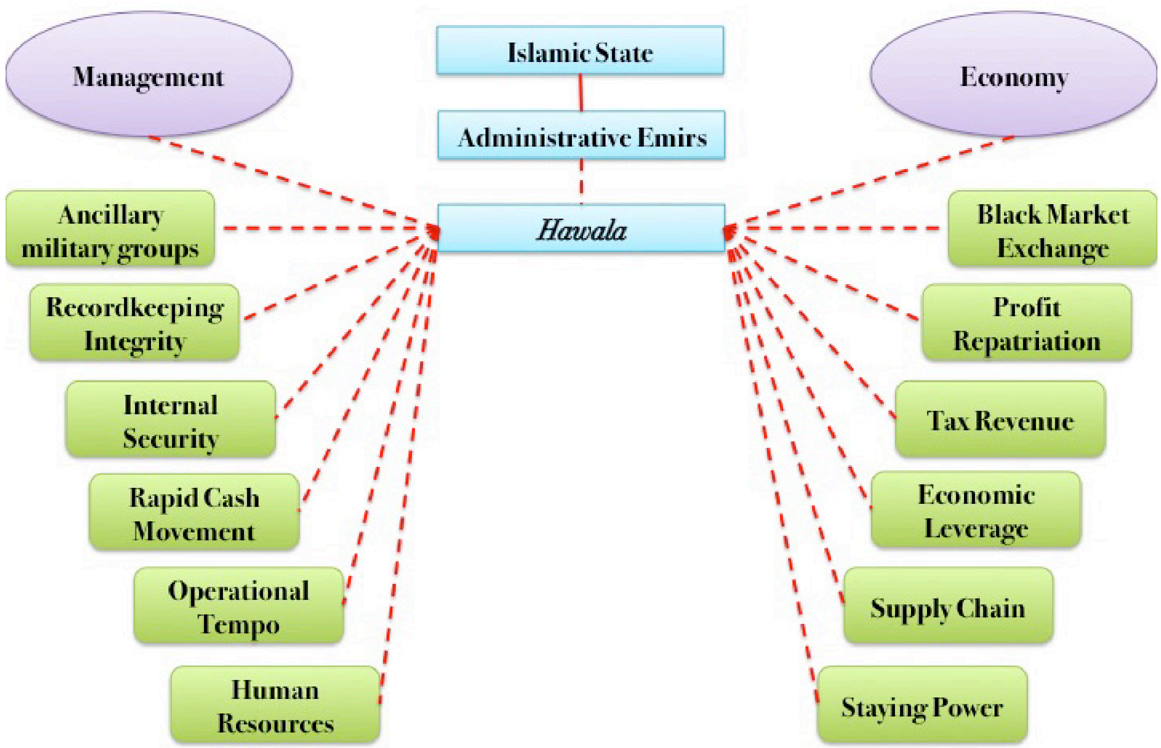
The Islamic State's partially decentralized network means that financial managers would have a high chance of functioning as the group's central most actors, and administrative emirs most clearly fit this description. As noted earlier, administrative emirs distributed funds across sectors, funded ancillary military groups, and collected data on members. They also maintained "daily revenues and expenditures for the provincial administration" (Bahney *et. al.* 2010, 8), individual member compensation rates (Johnston *et. al.* 2016, 156), and funded incidental expenses (Johnston *et. al.* 2016, 235). RAND even posited that certain record keeping anomalies found on one document could indicate that administrative emirs had knowledge of mid or senior level officials' aliases, wives/dependents, family names, and unit assignments (Johnston *et. al.* 2016, 170, 173-174, 180). This indicates that administrative emirs had a high degree of member, extra-group, and regional network connectivity, plus substantial financial responsibilities. Therefore neutralizing their activity would be key to disrupting the group's operations.

Figure 8: Administrative Emirs as Financial Managers



If this paper's contention that *hawaladars* are serving as administrative emirs or financial facilitators is correct, more attention should be given to engaging these actors as part of the broader counter-insurgency campaign to isolate and degrade the Islamic State's financial movements. The network of mutual trust would be broken if the Islamic State lost faith in a *hawaladar*'s promise of security and anonymity. Trust constitutes "the true center of gravity for criminal organizations," and "the spread of misinformation to discredit key figures and the disruption of criminal activities in ways which point to insider betrayal" could undo its foundation (Kan quoted in Williams 2015, 264-265). As both a terrorist organization and criminal enterprise, the Islamic State must contend with these vulnerabilities. Once network members are aware of a breach, the likelihood of additional members turning against their organization increases as the psychological cost of betrayal is lowered (Strang 2014, 24). Because *hawalas* exist and operate in a network, if the Islamic State lost trust in one link in the chain, it would be forced to reconsider its affiliation with the other links, degrading the group's efforts to build a strong informal economy.

Figure 9: *Hawala* as a Center of Gravity



<u>Conclusion</u>

The dearth of primary source documentation hampers comprehensive study of *hawalas.* Raphaeli (2003) states that the limited record keeping for *hawala* transactions and participants makes estimates on *hawala* transfer volume difficult (70). Keene states that *hawaladars* keep account of fees, exchange rates, customer *hawala* slips, customer identification, dates, invoices, receipts, contracts, invoices, and credit accounting. However, these records may be coded and are not kept long in regions where the institution is banned (Keene 2007, 190-191). Razavy and Haggerty (2009) say *hawaladars* maintain extensive records but these records are highly compartmentalized and could be unintelligible to non-participants (149-150). Thus, I echo the call from the RAND Corporation for a greater emphasis on acquiring terror financial and administrative records to "identify important nodes and techniques of internal communications and transactions, as well as higher-level insight into an organization's plans and strategies" (Johnston et. al. 2016, vxiii-xix). *Hawala* and exchange house records from within former Islamic State territories would provide unique insights into the group's criminal fundraising and black market exchanges. Since the Islamic State wanted reports on unit attrition levels, it is likely that *hawaladars* acting as administrative emir would have maintained detailed, intelligible records.

In the meantime, this paper adds to the discussion on *hawala* and terror finance by creating a theoretical framework for *hawala* functions in the Islamic State's informal economy and administration. It finds that *hawalas* are an Islamic State center of gravity, functioning as the foundation of the group's informal economy by facilitating oil profit repatriation, procuring weapons, and cementing the group's staying power vis-à-vis the formal sector. Although this paper cannot conclusively prove that *hawaladars* served as administrative emirs for the Iraq insurgency, it demonstrates the plausibility of such an arrangement by presenting a rationale from the standpoint of the insurgents. This theoretical exercise can benefit counter-insurgency officials seeking to understand *hawala* networks in Islamic State governance and the various players at work in the multidimensional landscape of the Iraqi conflict.

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