

## Conspiracy to Spy Novel: The Reza Zarrab Case and US-Turkey Relations

by Dilek Ulutaş

The new year has already given rise to tensions and recriminations in the US-Turkish relationship. Much of these revolve around the conflict in Syria, US and Western support for the Kurdish Democratic Union Party (PYD) and Turkey's sustained backsliding in democratic norms and freedoms, particularly pronounced since the failed coup attempt in July 2016.

A further, less publicized but highly significant dimension of these tensions stems from the arrest, in March 2016, of a well-connected Turkish-Iranian national in the US, accused of fraud, money laundering and assisting Iranian authorities to evade international sanctions imposed on Tehran in the context of negotiations over its nuclear programme.<sup>1</sup>

During the trial in New York, the defendant, Reza Zarrab, a wealthy

<sup>1</sup> Aslı Aydıntaşbaş, "The Zarrab Affair", in *ECFR Commentaries*, 24 November 2017, [http://www.ecfr.eu/article/commentary\\_the\\_zarrab\\_affair](http://www.ecfr.eu/article/commentary_the_zarrab_affair).

and well connected businessman with deep links in Turkey, agreed to become a state witness. His testimony implicated high-level Turkish ministers affiliated with the ruling Justice and Development Party (AKP) and the deputy general manager of the state-owned Turkish Halkbank in a scheme that allowed Iran to skirt sanctions and export its oil and gas reserves for gold, with some of the funds being moved through US financial institutions.

On 4 January 2018, the deputy manager of Halkbank, Mehmet Hakan Atilla, was convicted by the New York court on five counts of conspiracy, including conspiracy to defraud the US, setting the stage for a further showdown in Turkish-US relations as the US Treasury may now move to inflict heavy penalties on the Turkish bank.<sup>2</sup>

<sup>2</sup> Greg Farrell and Christian Berthelsen, "Turkey's Halkbank Could Suffer from Ex-Banker's U.S. Conviction", in *Bloomberg*, 4 January 2018, <https://www.bloomberg.com/news/articles/2018-01-04/turkey-s-halkbank>.

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Following the arrest in 2016, the Turkish government repeatedly called on the US to free Zarrab. The arrest was initially described as a politicized witch-hunt in Turkey, with Zarrab depicted as a “hostage” of worsening US-Turkish relations.<sup>3</sup> Last November, when news emerged that Zarrab had begun collaborating with the prosecution, Turkish authorities began denouncing Zarrab as part of an alleged plot to undermine Turkey’s AKP government.<sup>4</sup> By December 2017, Turkey moved to seize Zarrab’s assets in the country, with Turkey’s Prime Minister Binali Yıldırım being quoted in the media as stating that he hoped Zarrab would “turn back from his mistake” and end cooperation with the US prosecution.<sup>5</sup>

This is not the first time that Reza Zarrab faces scrutiny on charges of corruption and money laundering. Back in 2013, Turkish authorities arrested Zarrab during a corruption and bribery investigation involving illegal gold transfers and fake exports to Iran.<sup>6</sup> At the time, four AKP government ministers and some of their family members were also implicated in the investigation. Yet, the case was quickly

could-suffer-from-ex-banker-s-u-s-conviction.

<sup>3</sup> “Bekir Bozdağ: Reza Zarrab Being Held Hostage in the USA”, in *Cumhuriyet*, 20 November 2017, <http://www.cumhuriyet.com.tr/haber/english/870096>.

<sup>4</sup> “Zarrab Being Forced to Sign ‘Slanders against Turkey’: Deputy PM”, in *Hurriyet Daily News*, 27 November 2017, <http://www.hurriyetdailynews.com/zarrab-being-forced-to-sign-slanders-against-turkey-deputy-pm-123108>.

<sup>5</sup> “Reza Zarrab Case: Turkey Seizes Assets of Trader in US Trial”, in *BBC News*, 1 December 2017, <http://www.bbc.com/news/world-europe-42203274>.

<sup>6</sup> Fehim Taştekin, “Iranian Gold Stars in Turkish Corruption Scandal”, in *Al-Monitor*, 20 December 2013, <http://almon.co/1xck>.

buried and Zarrab walked free after a short stay in prison, with the Turkish government denouncing what it described as a Gülen-linked plot to undermine the AKP.<sup>7</sup> This decision is likely to come back and haunt the Turkish government as the New York court case is shining a new light on the 2013 probe, including the possible involvement of government ministers in the dealings with Iran.

Today, there is not only a risk of fines and even sanctions on Turkish banks. There is also the possibility of new prosecutions and arrests, as a result of the explosive revelations made public during the trial. Coming at a time when US-Turkey relations are already strained and tense, such revelations are adding further fuel to the fire and causing considerable political headaches in both Ankara and Washington.

Over the years, the US has fined many banks and financial institutions accused of money laundering and evading US or international sanctions. Most of these cases involved European banks, such as Deutsche Bank, ING Direct, BNP Paribas, Crédit Agricole and HSBC.<sup>8</sup> A number of US banks and institutions have also been charged. In these cases, however, banks agreed to a settlement and payed a hefty fine in order to avoid further public scrutiny

<sup>7</sup> Tim Arango, “Raids and Graft Inquiry in Turkey Are Seen by Some as Muslim Cleric’s Plot”, in *The New York Times*, 18 December 2013, <https://nyti.ms/2G11cbG>.

<sup>8</sup> “BNP Paribas to Pay \$9bn to Settle Sanctions Violations”, in *BBC News*, 1 July 2014, <http://www.bbc.com/news/business-28099694>; Jill Treanor, “Standard Chartered to Pay \$670m to Settle Iran Sanctions Allegation”, in *The Guardian*, 6 December 2012, <https://gu.com/p/3cb6c>.

and not run the risk of sanctions or being excluded from key financial hubs. The present case involving Halkbank is more problematic, involving a complex and murky scheme that allegedly saw the involvement of high-level bank managers and former ministers linked to the current AKP government.

During the trial, Zarrab testified that he had bribed Turkey's former Minister of Economic Affairs, Zafer Çağlayan, and also implicated Egemen Bağış, former Minister for EU affairs, in helping Zarrab set up a bank account with another Turkish bank, Aktif Bank, through which some of the dealings were allegedly made.<sup>9</sup> Resulting from these revelations, and notwithstanding some concern over the reliability of Zarrab's testimony,<sup>10</sup> the current investigation has mushroomed into a complex case that could serve as the script of a geopolitical thriller, complete with murky dealings between high level politicians, ministers and wealthy private citizens spanning three continents.

To make matters even more complex, a further set of uncorroborated revelations have emerged in which senior US citizens and politicians, including Michael Flynn, who briefly served as Donald Trump's National

Security Advisor, and Rudolph Giuliani, an influential lawyer and former mayor of New York, allegedly worked with Turkish officials and Donald Trump's presidential campaign to free Zarrab while seeking to bury the court investigation.<sup>11</sup>

Given the complexity of the investigation and the high political and economic stakes involved, it is likely that the full truth will never be revealed. Indeed, the fact that the trial has slowly become politicized, with it gradually becoming a source of domestic debate in the highly polarized domestic political battles currently underway in the US and Turkey, as well as within broader West-Turkey tensions, will likely result in a joint effort to limit the high-level political damage that could flow from the case.

That said, there are some real economic implications. The Turkish economy is already suffering from numerous internal and external challenges and the possibility of fines and sanctions on a major Turkish bank could have serious repercussions on Turkey's economic outlook. Notwithstanding high GDP growth in 2017, the annual inflation rate grew to 12.98 percent last November, the highest it has been

<sup>9</sup> Christian Berthelsen and Bob Van Voris, "Zarrab Takes Jury on Trip through a Sanctions-Evasion Plot", in *Bloomberg*, 29 November 2017, <https://www.bloomberg.com/news/articles/2017-11-29/gold-trader-zarrab-points-finger-at-atilla-at-sanctions-trial>.

<sup>10</sup> Benjamin Weiser, "Reza Zarrab, Taped in Jail, Said Lying Was Ticket to Freedom", in *The New York Times*, 4 December 2017, <https://www.nytimes.com/2017/12/04/world/europe/zarrab-turkey-iran.html>.

<sup>11</sup> Melik Kaylan, "The Zarrab Court Case: What It Means for Flynn, Trump, Erdogan, Even Putin", in *Forbes*, 5 December 2017, <https://www.forbes.com/sites/melikkaylan/2017/12/05/the-zarrab-court-case-what-it-means-for-flynn-trump-erdogan-even-putin>; Melik Kaylan, "The Zarrab Trial In New York Gives Up Its Secrets About Flynn, Giuliani, Erdogan: Part Two", in *Forbes*, 8 December 2017, <https://www.forbes.com/sites/melikkaylan/2017/12/08/the-zarrab-trial-in-new-york-gives-up-its-secrets-about-flynn-giuliani-erdogan-part-two>.

in 14 years.<sup>12</sup> Turkey's current account deficit has also increased, from 33.7 billion dollars at the end of 2016 to 41.9 billion dollars in early 2018.<sup>13</sup> The value of Turkish lira compared to the US dollar fell drastically in 2016, losing 17 percent.<sup>14</sup> This decline has a direct impact on the inflation rate and its debt repayment capacity. With municipal, national and presidential elections scheduled for 2019, the economy is likely to stand out as a major campaign issue. If Turkish banks are fined by the US Treasury, the AKP party may suffer at the polls, a dynamic that is sure to be keeping Turkish leaders awake at night.

But there may be more. Indeed, there are some worrying indications that US authorities may expand the investigative net, also involving other Turkish banks and institutions. Threats range from individual fines and sanctions to the potential that banks or financial institutions have their licence suspended, preventing them from operating in the US market or in US currency. Given that Zarrab has testified that different Turkish banks were involved in the transactions with Iran, there is a possibility that more Turkish banks become implicated in the probe. Such eventuality would pose economic but also political and even

geopolitical challenges for Turkey, the US-Turkey and West-Turkey relations.

In light of these developments, US and Turkish authorities would do well to redouble their efforts and quickly find an agreeable solution to the crisis. The risk is that tensions stemming from other developments seep over into the current investigation, politicizing its outcome and closing down room for potential compromise.

Halkbank will likely face a heavy fine and other senior members of the bank may join its deputy manager Atilla in facing US convictions. Ultimately, however, it is in the interests of both the US and Turkey to limit the political and economic fallout from the case.

While marred in significant tensions, the US-Turkey relationship, like the broader West-Turkey alliance in NATO, is too valuable (and fragile) to risk expanding the court case into high level political indictments of Turkish officials. Such an eventuality would effectively push Turkey closer to the Russian-Iranian axis and further complicate US and European interests in the economic, security and political domain, where important drivers of structural interdependence remain of significant benefit to both sides in the relationship.

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<sup>12</sup> "Turkey's Core Inflation Hits Highest Since 2004", in *Hurriyet Daily News*, 3 January 2018, <http://www.hurriyetdailynews.com/turkeys-inflation-hits-11-92-percent-in-december-2017-125146>.

<sup>13</sup> "Turkey's Economy Is One of the World's Fastest-Growing", in *The Economist*, 4 January 2018, <https://www.economist.com/news/europe/21734010-how-long-turkeys-economy-one-worlds-fastest-growing>.

<sup>14</sup> Roger Blitz, "Turkish lira falls to record low as higher inflation spurs selling", in *Financial Times*, 3 January 2017.



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