

Finance as a Tool of National Security: Update on the Effort to Combat Terror Financing

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Nov 29, 2007

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On November 29, 2007, Matthew Levitt addressed the Carnegie Council. Matthew Levitt is a senior fellow and director of the Stein Program on Counterterrorism and Intelligence at The Washington Institute. The following is a transcript of his remarks. A complete transcript of the event, including Carnegie Council president Joel Rosenthal's introductory remarks and the audience Q&A session, can be found on the Carnegie Council's [website \(http://www.cceia.org/resources/transcripts/0013.html\)](http://www.cceia.org/resources/transcripts/0013.html).

Thank you, Joel. I want to thank the Council for having me here again and all of you for braving actually relatively mild weather on this early morning.

I was going to start with the Gates quote too. I think it is extremely important that we have a Secretary of Defense who is speaking this way now. That is a very significant change. There is a lot that the military can do and there is a lot that it can't do, and to recognize that, coming from the head of our military establishment, is extremely, extremely important.

I'm actually not a very big fan of the term "war on terror," because I think it is very misleading, in that it suggests that a lot of what we need to accomplish can be accomplished by traditional military means. There actually is a role that the military plays in combating terror finance as well. They are very active. The Central Command (CENTCOM), in fact, came up with a term that I like to use instead of "terror finance" now -- and when I teach a course on the subject at Johns Hopkins, this is the term I now use -- "threat finance." What is meant by that is the financing of a traditional range of illicit activities, from terrorism, to proliferation finance, to insurgency finance; depending on their area of operations, perhaps counter-drug issues in Afghanistan as well.

That is important, in part, because even among terrorist groups that are not one and the same, even among disparate illicit actors that are involved in different types of illegal or illicit activity, you will find them using the same chokepoints, the same means of transferring funds, of laundering funds, and of storing funds in particular. Less so the same means of raising funds, but you will find that sometimes too.

Because of this, what I have argued for a long time -- and I believe that this in large part is the strategy that the U.S. government pursues when combating terror financing, in particular -- is that the biggest bang for our buck is not in focusing specifically on the fund-raising element of this problem. There will, unfortunately, always be new sources of funds for illicit purposes. There are enough people out there with access to funds that are radical or intend to do

harm. If you seize some of those funds, fantastic. Financial measures have a great disruption potential.

But you will have the biggest bang for your buck at that middle section -- not at the raising section at the beginning, but at that middle big section of transferring, laundering, and storing funds -- first of all, because you will find these chokepoints.

So when sometimes people say that combating terror financing is not very effective because we haven't seized a whole lot of money -- which is true, in the scope of things we haven't seized all that much money -- they are missing the point. Sometimes we are not even trying to seize as much money as we can; we are trying to shut down key chokepoints. A chokepoint -- a charity, an individual when designated -- may not even have in its accounts at that given time a whole lot of money, and yet may have a disproportionately large disruption impact by virtue of having been a key chokepoint. Sometimes that is something that will be able to be disclosed in the declassified public statements that the Treasury Department puts out, and sometimes it won't.

Parenthetically, when the Treasury Department right after 9/11 first started engaging in these designations, they didn't put out any information. Right after 9/11, there were just lists: "These are the people who are banned, these are the people whose assets have been frozen. Thank you very much. Have a nice day."

You can imagine the sensitivities within the intelligence community about putting sources and methods at risk. Much of the information underlying those designations is classified. A significant part of my job as Deputy Assistant Secretary for Intelligence and Analysis at Treasury was playing that interagency role, as a member of the intelligence community and as a senior member of the Treasury Department, finding some useful information from the significantly thick underlying evidentiary package for each of these actions that can be shared publicly so as to inform why we are doing this and what it is all about. I think that is an extremely important thing to do.

I will add, parenthetically, that I don't think we do enough with it. If I still have bruises on my face, it's because of those interagency battles about "Is this sensitive? Is it too sensitive? Can we declassify it? Do we need to declassify it? Why do we need to tell anybody anything?"

My feeling is that on the financial war on terror, and really all other aspects of the war on terror, the one area where we are least successful, where I would argue we really haven't fully stepped into the ring, is in the battle of ideas, in strategic counter-terrorism, in counter-radicalization. The Department and the intelligence community go to such great lengths now -- and it is a painful process -- to declassify material, and I don't think they do enough with it.

It's as if, as I've teased some of my former bosses at the Department, they assume that people wake up in the morning and have a lovely cup of coffee and run to their computers to see if there's anything new on Treasury's Web site. There has to be more that is done.

Now, I was very, very pleased that when the Department took a series of robust actions against Iranian entities a few weeks ago -- some for connections to terrorism related to Iran's Quds Force, more related to proliferation -- I was very pleased with the public diplomacy effort that they did there. I spoke to some people in the Treasury Department, in the State Department, and elsewhere, and this really was a concerted effort on their part to improve that system. So there is a lot of hope there, and I think that is very important.

But terror financing is only one part of it. There are two sets of metrics. Neither of them is particularly useful. As I mentioned, mentioning how much money has been frozen is not particularly useful. Measuring how many entities have been designated is equally un-useful, because there are many, many reasons why a known entity, an entity that is known to be financing terrorism, would not be designated.

First of all, there are all kinds of interagency equities in this process. You may come to the table, and even if you get everyone around the table to agree that the information indicates that this is a good target for designation, the State

Department may say, "Let's put this on hold for a little bit because we are trying to negotiate a peace deal between these two rival parties in this region." Or the intelligence community may say, "We have or are close to getting a great penetration of some sort and we don't want to put this potential source and method at risk." Or the law enforcement community may come and say, "We are actually about to indict someone or the Belgians are about to indict someone. If they come to us, we don't want to seem to be prejudicial."

There are all kinds of reasons why it doesn't happen. And that's okay because -- and I find myself saying this over and over and over -- we tend to mistake those things which are most public, such as Treasury designations and Department of Justice prosecutions, for the sum total of our counter-terror finance toolbox, when in fact it is only the most blatant tool in the toolbox.

But as you heard, there are multiple tools in this toolbox. We are not the plumber who comes to fix the sink with only a hammer. There are financial intelligence activities that are going on. There is a lot that the diplomatic community and the State Department can do in foreign trading, cross-border courier interdiction, programs that are proving very successful.

That is really important, because terrorists are no longer most dangerous because they are revolutionary; they are most dangerous because they are evolutionary. One of the downsides to providing all this public information is that we are showing our hand in some part, and they are much quicker to change than we are. Having been in this bureaucracy twice now, believe me, it is very slow to change. Even when it knows what needs to be done and even when it knows how to do it, it is slow to change. And they are very, very quick to change. There is no red tape. So if we shut down one type of means of transfer, they will move to another and we need to play catch-up.

Does that mean that this is not a useful technique? I argue no. It is an extremely useful technique. It is very useful in terms of disruption, which to me is what counter-terrorism is all about.

When I testify on the Hill before Congress, I am often asked, "So when are we going to win the war on terror?" That's the first reason I don't like that term, because it suggests at some point I'll be able to say, "We won, that's it."

Really, counter-terrorism is about constricting the operating environment. There are always going to be people who want to do us harm for political reasons, and at its heart that's what terrorism is. The question is: can you get it down to a reasonable level and can you make it harder for them to do all the things they need to do, from procuring false documents and raising, laundering, and most importantly getting, money when they need it where they need it? If we can constrict the operating environment, we can make some great success in counter-terrorism.

Following the money is a very effective tool. Also, sometimes you follow the money and sometimes you freeze the money. There is a tension there, an ongoing debate, in any given case whether you should freeze these funds or follow these funds. There is no "Jack Bauer moment," for those of you who watch "24," a show that my oldest son loves, this counter-terrorism show with this FBI agent who always knows what's going to happen where. There is no "Jack Bauer moment."

But there are some cases where financial intelligence has proven extremely effective in thwarting plots, most recently and most importantly, the Heathrow bomb plot that led to my having to put my little toothpaste in a Ziplock when I came here yesterday.

But as I said, we are dealing with a threat finance issue, not just terror finance. That's one part of the problem.

I think that one of the most interesting and creative issues that we have been tackling now is on the counter-proliferation side of this equation when it comes to Iran. Here there is a great misunderstanding of what Treasury has done, a very creative way to apply what are traditionally called sanctions, but we don't like to use that term because it's loaded and often considered a dirty term. Sanctions are often affiliated with the kind of shotgun,

countrywide sanctions that were applied against Iraq with, let's be honest, no success.

Whereas what we are applying now we prefer to call "targeted financial measures," because they are targeted on illicit behavior. It is made very clear "here is the illicit behavior that has to change for these sanctions to be removed." They are graduated -- you don't go from zero to 60 right away; you don't do everything that you could possibly do under the sun, because you are trying to change behavior.

But in order for a graduated sanction to work, you have to follow through with your threats. It's like me and my children: If I tell them there's going to be a consequence to bad behavior, that consequence has to happen if that bad behavior is done so that they understand that I mean it when I say it.

This is why it is so critical for there to be a third UN Security Council resolution targeting Iran. Because to be effective, we can no longer afford to be so targeted and so limited and graduated in our steps, if we then don't follow through when Iran thumbs its nose and doesn't change its illicit behavior.

Now, there are two types of actions that are being taken here, and this is where the misunderstanding tends to happen.

The first are offense tools. I would put the terrorism designation writ large into this category.

I would also put the majority of the designations under proliferation executive orders under this category as well. This is basically the category of when you know that there is an illicit actor engaging in some type of financing for illicit activities, the Treasury Department has an obligation to take offensive measures to try to deny them access to the international financial system. There is one international financial system today. Even with the dollar where it is, embarrassingly beneath the Canadian dollar even, we are still at the very center of that international system. I'll get back to that in a second.

I think most people understand these offensive tools, mostly through executive orders that empower mostly the Treasury Department, in some cases the State Department, to take these offensive actions.

But there are also defensive tools that the Department has and defensive responsibilities that any finance ministry has to protect its market -- I used to say "currency"; maybe that's not so accurate anymore -- but really to protect our currency too from abuse.

That's what the Department did in the North Korea case with Banco Delta Asia. People tend to compare the North Korean and the Iran cases all the time. There are some things where the comparisons make sense. Here they don't.

North Korea was not an offensive action; it was a defensive action. We found that there was a bank, Banco Delta Asia, that was holding on to a relatively small amount of money, about \$24-25 million, for the North Korean regime, which we later found out was money that was personal Kim Jung Il funds and, therefore, touched a raw nerve with him, and I think that's in large part what it was so successful.

But the issue was that this bank was taking an extra premium to literally look the other way when money that it knew was coming from the proceeds of counterfeit funds, cigarette smuggling, all kinds of different fraud, was being deposited in the bank -- literally, "Here's a little extra wad of cash; now you please leave the room."

If you are a risky actor, we, the United States, need to weigh whether or not we can afford to let you be a player in the U.S. financial system, whether your entree into the system could hurt our system. That's a defensive measure; that's not an offensive measure. "You decide to engage in risky, illicit, illegal behavior, I may not be able to let you into New York." When it comes to banks, they want a branch in New York, if for no other reason than their desire to dollarize transactions.

P.S. From the very first moment of Iran sanctions many years ago, the Treasury Department created a loophole

enabling Iranian banks to dollarize their transactions, even though they are not allowed to deal with American banks directly, through third-party banks -- say, European banks, Deutsche Bank, Credit Suisse, et cetera -- not out of any generosity to them, but because it was in our interests to make sure that the international oil economy remained dollarized. But they are able to do that -- Credit Suisse, Deutsche Bank, et cetera -- because they have a branch here in New York.

So when we say in the case of Iran to banks, for example, "Look at Banco Delta Asia. Understand that if you continue to engage in business with Iran, forget the fact that it is a regional and an international security threat. Just think about the investment risk. When we give you that information and you continue to do business with them, we may have to take defensive measures."

Now, the banks often see this as an offensive measure, as punishment. I have had these conversations with major banks as a senior Treasury official, and I am often sought out now by these banks, as a former Treasury official, to kind of explain what is going on.

My message to them is as follows: "When it comes to Iran, the Department has gone to great lengths to explain to the financial sector that there is an inherent investment risk to Iran. How can you be sure that money you are investing in Iran, loans you are providing, lines of credit you are providing, are not being used for alternative purposes?"

"Iran claims to have a financial intelligence unit, but it does not. Iran claims to have an anti-money-laundering regime; it does not. The Department has declassified intelligence that Iran does have a nine-digit line item in its budget for terrorism support. And it has declassified several instances where banks like Bank Saderat, Bank Sepah, Bank Melli [all Iranian banks] were engaging in deceptive financial transactions, hiding the nature of their and Iran's footprint in a transaction that was to support illicit activity."

That's the kicker, that's when I get the compliance officer's attention, because the best compliance regime in the world will never raise an eyebrow if a transaction looks like a telecommunications company in Turkey is making the transaction. They will have no way to know that this is actually a nuclear or ballistic missile program transaction from Iran.

Deceptive financial transactions are the key, because financial institutions understand that there are market forces at play forcing their hand. It's not the Treasury official -- I'm just providing the information. They have reputational risk. They do not want to be on the front page of The Wall Street Journal or Financial Times tomorrow morning for having continued to do business with an entity despite all the risks that they were told about. They have fiduciary obligations to their shareholders and they have due diligence requirements.

Based on those three prongs, you then look them in the face and say: "What confidence can you possibly have, given these deceptive financial transactions, that the money you are investing, the lines of credit you are providing, are not being used for all this illicit activity we know about?" The answer is they can't. They have answered their own question.

You can't overplay your hand. You have to be very careful. Not only in the case of Iran are we dealing with the international oil economy, Iran is obviously at the total opposite end of the spectrum than North Korea when it comes to not only the type of country but the type of economy -- totally closed, totally open; completely unintegrated, completely integrated -- but when you sit down on a regular basis and analyze what is the best tool to deal with this problem of the various financial tools that we have and are any of the financial tools even among the best tools to be used, you can do some really interesting and creative things. That's what's being done now.

What gives me the greatest comfort is that people are thinking smart. You don't have departments saying, "Well, I have these tools and I feel the need to flex my muscles. Let's use my tool." You actually have people sitting down and discussing what's the best tool.

You will notice in these recent designations of Iranian entities some were done by the State Department, some were done by Treasury, and there are mild differences that I won't bore you with and why. That was very interesting. Some were based on terrorism support. Some were based on proliferation support.

There are other things that can be done. When this concludes, we can have more of a discussion.

For example, I think it is important that others in the international community start having similar discussions with the private sector, much like the U.S. Treasury Department has had. The U.S. Treasury officials have gone out to the Middle East and to Europe and to Asia and they have met with the private sector, and with the governments as well, and not behind the governments' backs.

I think it would be extremely powerful, for example, if London, which is often considered with New York as the two twin power centers, had similar conversations, which is something Her Majesty's Treasury is considering.

I think if there were other segments of the business community, not just the financial community, with whom we started having these types of conversations, there could be other types of utility. Even if it was just making Iran know that we are having conversations with the shipping insurance industry -- not so much to talk about the risks of underwriting the shipping of oil out of Iran, because to be honest, from a selfish perspective, oil is expensive enough -- but how about if we started talking about the risks of shipping back to Iran the refined oil that they have to re-import because they do not have a sufficient refining capacity at home? Iran re-imports 40 percent of its domestically consumed oil.

There are leverage points here. If they are applied wisely, and if they are applied in an effort to change behavior, not just punish, and those behaviors are clearly articulated, we will continue to have a tremendous amount of not only transatlantic but international support.

There are very specific reasons why Russia and China are not yet onboard, and I believe that it may not be the third UN Security Council resolution we'd all like to see -- that I would like to see -- but that there will be something, and that that in and of itself will be telling, because the political message to Iran, that even Russia and China are onboard, is in large part, or at least in part, one of the most important messages of the previous two UN Security Council resolutions.

I think that the U.S. sanctions on Iran a few weeks ago targeting a whole host of actors, including banks, including companies tied to the oil industry that are also tied to the Revolutionary Guard Corps [IRGC], in large part was a menu from which the international community has been invited to select a few targets that it can agree upon, one or two targets. Even if, I would argue, it is just one bank, and put that in a UN Security Council resolution, that would be very, very effective.

There is a lot more than can be done here. We haven't solved the problem, and this tool will not solve the problem.

With this I'll conclude. People ask me all the time, "Are sanctions going to solve the problem?" The answer is no, certainly not on the proliferation side. It is disruptive on the counter-terror finance side. And no one suggests it is going to solve terrorism. It's disruptive.

On the counter-proliferation side, I argue that all it is intended to do is to create space for diplomacy, to create leverage for diplomacy. That's what sanctions that are focused on illicit actions, on changing behavior, are all about.

At the end of the day, I do believe that you need to have a credible military option -- which, God willing, we will never have to use at any level -- and we have to have a soft power option that is firm but soft, and I think that is where the financial angle comes in. At the end of the day, this, like basically most other international problems, will be solved only through not soft diplomacy, not mushy diplomacy -- we're not going to go to Tehran and ask them "would you please?" -- but it will be solved through very aggressive diplomacy that is backed up by very firm financial

consequences, and perhaps a carrier in the Gulf that implies other consequences, that forces people to sit down at the table.

I am very, very pleased and honored that you have chosen to sit down at the table with me this morning. I hope that you have some targeted questions for me. ❖

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