The Role of Finance in Combating National Security Threats

May 10, 2007

In-Depth Reports

On May 10, 2007, Robert Kimmitt addressed The Washington Institute's 19th annual Soref Symposium. Ambassador Kimmitt is deputy secretary of the treasury. The following is the prepared text of his remarks.

Read (https://www.washingtoninstitute.org/templateC05.php?CID=2605) a summary of the audience Q&A session following Ambassador Kimmitt's address.

Thank you very much, Peter. It is a pleasure to join so many distinguished guests this evening, including Ambassador Dennis Ross, a friend and colleague for more than 20 years.

When reviewing what previous speakers had said to this august group, I noted that two years ago Paul Wolfowitz told a story about Ambassador Dick Walters, with whom we had both served during the Reagan Administration. Dick Walters was subsequently my predecessor as Ambassador to Germany, and he gave me just one bit of advice before I left for Bonn in the summer of 1991: "Don't ever forget how important speeches are to the Germans. They like to give speeches, listen to speeches, and analyze speeches far more than is the case in the United States." He recounted a story of speaking once to a distinguished group like that assembled here. He spoke in his excellent German for 40 minutes and sat down, rather pleased with himself, only to have the host of the evening stand and say, "Mr. Ambassador, thank you for your remarks. If you ever have time for a real speech, please come back to see us again." Well, if 40 minutes is when a "real speech" starts, you will be receiving from me tonight only remarks -- no more than 30 minutes -- so that we can leave time later for your questions.

Like so many others, I have benefited significantly from the work of the Washington Institute. In addition to reading your excellent analysis and research on a regular basis, I have also come to appreciate that the Institute and the Treasury Department engage in an informal, but mutually beneficial "exchange program," as some of our best and brightest spend time in each organization. In fact, two former Treasury colleagues, Matt Levitt and Mike Jacobson, are here with us this evening as they continue their superb research in your organization, and we are also joined by several current Treasury staff members.

I would like to discuss with you tonight the new and important role of the Treasury Department in combating national security threats. It is hard to imagine that we would have had a conversation like this when the Washington Institute held its first Soref Symposium event in 1988. It is only in recent years that the challenges of counter-terrorism and counter-proliferation have moved beyond the traditional province of foreign affairs, defense, intelligence, and law enforcement. Treasury and other Finance Ministries around the globe have evolved since September 11th, and the world of finance now plays a critical role in combating international security threats.

Treasury Transformed

In this new era, the Treasury Department is uniquely positioned to help address threats to global peace and security. This evening, I will outline how we have transformed our Department in order to detect, disrupt, and where possible, dismantle illicit financial networks. The Treasury Department has drawn upon its full range of authorities to target state sponsors of terrorism and WMD proliferation, in particular the Iranian regime, and we have coupled these domestic actions with coordinated multilateral efforts and engagement of the international financial community.

Our strategy today is notably different than it was during my first tour at the Department in the 1980s, when I served as Treasury General Counsel during the second Reagan term. During those years, the Treasury Department was rarely involved in high-level National Security Council discussions -- at most, perhaps five or six times a year. Today, Treasury is represented at five or six NSC meetings a month, both on the positive side of our agenda -- helping stand up the economy in Iraq, for example -- but also on the punitive side, where we seek to constrain illicit conduct by Iran, North Korea, and others.

To discharge these important responsibilities, the Department has developed new organizations and authorities to target key transnational security threats. In 2003, Treasury created a specific office dedicated to targeting the financial underpinnings of terrorism. This office was the beginning of a transformation within the Department to leverage existing capabilities to safeguard the financial sector from corrupt activity and play a more strategic role in combating terrorism. The following year, congressional and Executive action expanded this effort by creating the Office of Terrorism and Financial Intelligence, or "TFI" for short. TFI's mission is groundbreaking: it enhances the role of Treasury beyond pure economic and financial matters to include the development of innovative means to combat asymmetric, borderless threats. One of the clearest examples of this innovation at the Department is the creation of an in-house intelligence analysis office to bring the knowledge of the intelligence community to bear on the evolving threat of illicit finance. This office, the first of its kind in the world, helps Treasury enhance national capabilities by enabling our analysis of financial networks and infrastructure to be disseminated throughout the intelligence community.

With these expanded capabilities, the Treasury Department is uniquely equipped to address threats to our national security with a wide range of domestic legal authorities. Some of our tools are defensive measures, such as Section 311 of the USA PATRIOT Act, which authorizes Treasury to designate as a primary money laundering concern either a foreign jurisdiction, financial institution, type of account, or class of transactions. Section 311 enables Treasury to impose a range of special measures that U.S. financial institutions must take to protect against illicit financing risks associated with the designated target, including cutting the entity off from the U.S. financial system. Other authorities, such as the International Emergency Economic Powers Act (IEEPA) -- which I will discuss further -- are more offensive in nature. These authorities are mutually reinforcing: we use both our offensive and defensive authorities to enhance and protect the ability of governments and the private sector to combat threats to the international financial system.

We have also led the effort in the international community to combat illicit financial activity. The Treasury Department's Office of Terrorism and Financial Intelligence leads the U.S. delegation to the Financial Action Task Force (FATF), a key international organization where finance ministries, central banks, and regulators meet frequently to share information and best practices, and set global standards for combating terrorist financing and money laundering. FATF works to establish standards to counter illicit financial conduct within the international community, and these standards -- which have also been incorporated into the programs of the World Bank and the IMF -- aid countries in developing their own specific anti-money laundering and counter-terrorism financing laws and regulations.

Through FATF's working groups and its regional bodies -- which include more than 150 countries -- TFI's typologies have spurred the creation of new guidance materials and best practices that outline methods for countries to implement counterterrorism financing and anti-money laundering standards. For example, the United States led international efforts to examine the abuse of non-profit organizations for terrorism financing purposes, and launched a study regarding the use of cash couriers as a means for moving funds in support of terrorism and other illicit activities. This study led to concrete actions by countries around the world to address the implementation of disclosure and declaration requirements for moving cash across borders.

We also led efforts within the FATF to address WMD proliferation by creating a mechanism to target proliferation finance and develop authorities to isolate WMD proliferators and their support networks. Through these efforts, we have worked to broaden the scope of traditional financial regulation to include law enforcement, intelligence, and policy coordination. This multi-faceted approach to financial crime creates a broad impact and has resulted in broader adoption of FATF standards -- effectively enhancing counterterrorism efforts around the world.

The issue of countering terrorist and proliferation finance is also now firmly on the agenda of other international organizations such as the United Nations and the European Union. At the United Nations, nearly every UN Security Council resolution that has been passed since September 11th, including all those designed to counter WMD proliferation and terrorism, contain financial provisions -- from obligating states to perform enhanced scrutiny of financial transactions to the freezing of assets. In addition to the World Bank and IMF, other major international financial and economic forums, including the G-7, G-8, and APEC -- the Asia Pacific Economic Cooperation -- are also examining these issues. The G-20, an increasingly influential group of countries that includes China, India, Brazil, Australia, Turkey, Saudi Arabia, South Africa, and Mexico, has also become more involved in combating illicit finance.

With strengthened domestic authorities and increased international action, the United States is now much better equipped to address the threats facing a globalized world. The question then remains -- how do we use these tools most effectively? When we consider the best use of sanctions, many of us remember all too well Cold War-era sanctions, which often put only moderate pressure on the Soviet Union but resulted in increased tensions in transatlantic relationships. In fact, in 1983, one committee of academics, business leaders, and opinion makers described American economic sanctions against the Soviet Union in this manner: "Two things are of significance above all others: one, they haven't worked; two, they can't work."

To avoid past problems and increase effectiveness, we have developed a smarter, more focused sanctions approach. Specifically, the United States has worked to apply targeted financial pressure to isolate individuals, entities, and regime elements engaged in illicit finance in support of terrorism or WMD proliferation. These financial measures are aimed not at countries in general, but at conduct in specific. Applying effective financial sanctions requires careful economic, legal, and policy analysis to ensure that the measures are calibrated to meet their goals and minimize unintended consequences. The objectives for these measures are to isolate the target as well as to induce it to abandon harmful policies or practices. As David Ignatius aptly put it, "these new, targeted financial measures are to traditional sanctions what Super Glue is to Elmer's Glue-All."

Some of these targeted measures require financial institutions to freeze funds and close the accounts of designated actors, effectively denying these actors access to the traditional financial system. Other measures impose bans on travel or arms transfers, serving to isolate the target. These kind of measures have several advantages over broad-based sanctions programs. Most importantly, instead of designating an entire country, they single out those responsible for supporting terrorism, proliferation, and other criminal activities, and such targeted measures are more likely to be accepted by a wider number of international actors and governments.

Iran

Turning to the subject of Iran, the Washington Institute has continued its excellent, incisive work on the Iranian regime, including during this symposium. The title of your event is precisely correct -- the prospect of an Iranian bomb is unacceptable, not just to the United States but to the entire world community, as evidenced by two unanimously adopted UN Security Council resolutions requiring the Iranian government to cease uranium enrichment. Iran's unrelenting pursuit of a nuclear weapons capability, combined with its continued provision of financial and material support to terrorist groups, makes the possibility of a nuclear-armed Iran a direct and dangerous threat to the international community.

To address the Iranian threat through deterrence and prevention, the United States has employed a two-fold sanctions strategy: utilizing domestic authorities and engaging in international outreach.

First, under the International Emergency Economic Powers Act, which provides broad statutory authority to respond to threats, the President issued Executive Order 13382 in 2005. This Executive Order authorizes the Treasury and State Departments to target key nodes of WMD and missile proliferation networks, including their suppliers and financiers, in the same way we target terrorists and their supporters. A designation under Executive Order 13382 denies the targeted entities access to the U.S. financial and commercial systems and puts the international community on notice about the threat posed to global security. These prohibitions have a powerful effect, as the suppliers, financiers, transporters, and other facilitators of WMD networks tend to have commercial presences and accounts around the world that make them vulnerable to exactly this kind of financial action.

The United States designated the Iranian state-owned Bank Sepah under E.O. 13382 for providing financial services to Iran's missile program, and this action has had a significant impact. Like other Iranian banks, Bank Sepah engages in a range of deceptive practices in an effort to avoid detection, including requesting other financial institutions to conceal the Sepah name when processing its transactions in the international financial system. Additionally, Bank Sepah has facilitated business between North Korea's chief ballistic missile-related exporter, KOMID, and Iran's Aerospace Industries Organization. KOMID, which has also been designated by the Treasury Department under E.O. 13382, is known to have provided Iran with missile technology. By cutting off Sepah from the U.S. financial system, we have commercially isolated the institution and have made it more difficult for Iran to finance its proliferation-related activities.

Second, we have also worked through the international community to build upon our domestic actions. We are most effective when we proceed multilaterally, either with a coalition or with the consensus of the United Nations. Our multilateral efforts have yielded critical success in the fight against proliferation financing, and a key example is the unanimous adoption last month of UN Security Council Resolution 1747, which reaffirms and expands UN Security Council Resolution 1737 of December 2006. These resolutions target Iran's nuclear and missile programs, and among other requirements, obligate states to freeze the assets of named entities and individuals associated with those programs. Significantly, among these entities was Bank Sepah. The United States has worked with governments and financial institutions around the world to implement the common obligation to freeze the assets and economic resources of all listed entities and individuals, including Bank Sepah and Bank Sepah International.

We have worked closely with our fellow finance ministries and central banks abroad to build consensus on these financial measures, and the effect has been striking: international partners who originally resisted the idea of applying sanctions on Iran have reversed this position and now support pressuring the Iranian regime to renounce its support for WMD proliferation and to comply with its international obligations.

This is especially significant because we believe that segments of Iranian society beyond President Ahmadinejad and the Islamic Revolutionary Guard Corps -- including the mullahs, their merchant class backers, and liberalizing forces -- understand the high costs of the country's increasing isolation and the need to change its behavior.

Engaging the Financial Community

Our multilateral action to change Iran's behavior is not confined to governments, however. We have engaged in unprecedented outreach to the international private sector, meeting with more than 40 banks around the world to share information and discuss the risks of doing business with Iran. We exchange common interests and objectives with the financial community when it comes to dealing with threats. Financial institutions want to identify and avoid dangerous or risky customers who could harm their reputations and business, and governments want to isolate those same actors and prevent them from abusing the financial system.

We are seeing concrete benefits through this partnership. We have learned that the Swiss bank UBS cut off all dealings with Iran, and Credit Suisse and HSBC have also significantly limited their exposure to Iranian business. A number of other foreign banks are refusing to issue new letters of credit to Iranian businesses. According to the banks, these were business decisions, pure and simple - handling Iran's accounts was no longer good business. Multinational corporations have also held back from investing in Iran, including limiting investment in Iran's oil field development.

Further, in a move that demonstrates that Iran is feeling the effects of financial isolation, the Iranian government also filed a complaint with the IMF -- subsequently denied -- that U.S. action against Bank Saderat, an Iranian state-owned institution, constituted a foreign exchange restriction.

And last year the OECD raised the risk rating of Iran, reflecting this shift in perceptions and indicating its sense of the inherent risk in doing business with Iran. Governments should not subsidize via export credit programs the country risk created by Iran's illicit behavior. The good news is we have seen a sharp decrease in export credits from countries such as Germany, France and Japan. We expect that the OECD's higher risk rating will contribute to a continued downward trend in export credits to Iran.

Additionally, Iran recently announced that it has reallocated its foreign reserves out of dollars. This raises the important point that while a growing number of banks have cut off Iranian business in dollars, they have not yet done so in other currencies. Regardless of the currency, the core risk with Iranian business remains the same: when dealing with Iran it is almost impossible to "know your customer." Since banks cannot be certain that parties are not involved in illicit activity -- and such conduct is not limited to one currency -- scaling back dollar-business reduces the problem, but does not eliminate it.

In spite of these successes, some have asked if further measures should be considered to increase pressure against Iran. Members of Congress are considering a number of legislative options, including application of U.S. sanctions to the business activities of foreign subsidiaries of American companies; mandatory divestment from companies doing business with Iran; and having the government "name and shame" firms -- both domestic and foreign -- that do business with Iran. While these proposals are certainly well intended, they could have significant counter-productive policy implications. Our shared goal is to pressure the Iranian regime to change its behavior, and the best way to achieve this objective is to keep the focus on illicit conduct and maintain as broad an international coalition as possible. Yet many of these proposed measures may be seen by our allies as extraterritorial U.S. Government action and could affect our ability to obtain their cooperation on mutual action with respect to Iran.

You might recall the history of this debate. In the 1990s, for example, we were concerned about the commitment of our allies to put pressure on Iran through the imposition of sanctions. The European Union, in turn, argued that some measures under consideration were an inappropriate extension of U.S. law. In recent years, as discussed earlier, our economic sanctions strategy has evolved into a more targeted and conduct-based approach. Along with our international outreach, this has helped to build a coalition of partners with a shared goal of putting as much pressure as possible on the Iranian regime to change its behavior. As Mike Jacobson pointed out in a recent Washington Institute policy paper, our economic sanctions against Iran are intended to engage, not confront, our allies. We must be careful not turn this successful effort into a debate that would engender transatlantic friction and turn the focus away from Iran's illicit conduct. Sanctions have the most comprehensive impact when applied cooperatively and collectively.

In closing, let me make clear that the Treasury Department's objective is to employ the most effective methods to dissuade the financing of dangerous activities, and especially Iran's nuclear ambitions.

After 30 years of experience in national security policy, I have come to the conclusion that the most effective sanctions meet the following criteria: they are carefully targeted at illicit conduct; they are multilateral in scope; and they engage financial and business institutions as well as foreign governments. Any additional sanctions proposals should be judged against these criteria to ensure maximum effectiveness in deterring Iran's dangerous behavior. We look forward to continuing to work with all who support this goal, including the Washington Institute.

Thank you for your kind attention, and I look forward to your questions. ❖

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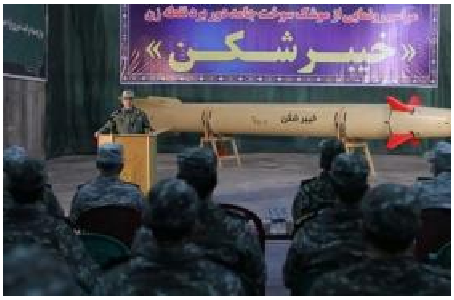

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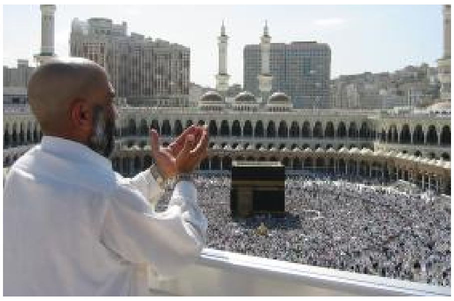

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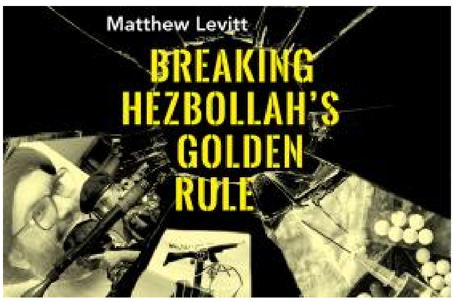

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