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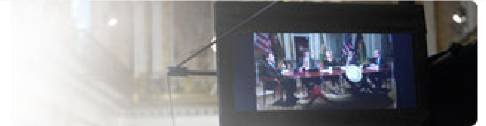

Remarks of Under Secretary for Terrorism And Financial Intelligence David S. Cohen at The Practicing Law Institute's "Coping With U.S. Export Controls And Sanctions" Seminar, "The Evolution Of U.S. Financial Power"

12/11/2014

As delivered

WASHINGTON - Good afternoon. Thank you, Chris, for that kind introduction, and thank you to the Practicing Law Institute for having me here today. I spent 20 years practicing law before I entered the Obama Administration in 2009, so it's a real pleasure to be back among my people.

The subject of this conference is "Coping with U.S. Export Controls and Sanctions." I recognize that, from where many of you sit, our sanctions and export control requirements are, indeed, things to be coped with.

But I also know that government and industry both share deep commitments to the integrity and stability of the global economy. When an aggressor state, terrorist group, transnational criminal organization, or nuclear proliferator threatens to undermine international peace and stability, it is in everyone's interest that the United States makes use of all available tools – especially our non-kinetic tools – to respond. Indeed, before we put troops in harm's way, we have an obligation to exhaust all other viable options. And when we deploy our military, we need to mobilize all elements of national power to give our forces every advantage on the battlefield.

Because of the hard work and cooperation of many in this room, and many of your employers and clients, we have been able to leverage the strength, resiliency and attraction of the American economy and financial system to advance our national interests. So let me begin by thanking you for being here, and thanking you for your partnership in achieving these important goals.

Over the course of these two days, you'll hear from some of my colleagues across the U.S. government and have the opportunity to drill down into the specifics of U.S. sanctions and export control policies.

So this afternoon, I thought I would take a step back and offer a few thoughts on how our sanctions toolkit has evolved in recent years, why we choose to rely on those tools, and why I think we have gotten more creative in developing and deploying them. And because this is a trade-focused conference, I specifically want to talk about how and why we have transitioned from broad trade restrictions to more targeted, and often more potent, financial measures.

From Broad Embargoes to Targeted Sanctions

Over the past decade or so, one important way that the United States has protected our nation's core interests, projected power, and exercised leadership on the world stage is through the increasing use of financial measures. Far from just focusing on terrorist financing and money laundering, my office in the Treasury Department is now regularly called upon to help advance a variety of U.S. national security and foreign policy goals.

This is partly because not every national security challenge is best met through military means. Last spring, speaking to the graduating class at West Point, President Obama reminded the new officers that, "Just because we have the best hammer, does not mean that every problem is a nail."

But it's also because financial measures have become far more powerful tools of statecraft, and their effects are multiplied in a world defined by economic interdependence. Let me begin with a story that I think illustrates just how far we have come.

It was 1807, and President Jefferson had a decision to make. The Napoleonic Wars were raging in Europe, and the United States found its sailors constantly harassed by the British Royal Navy on one side and France's Marine Nationale on the other. Jefferson desperately wanted to keep America out of war, but he also wanted to push back against the European powers for their brazen attacks on U.S.-flagged ships. When diplomacy alone did not suffice, and with military options particularly unappealing, Jefferson decided to leverage U.S. economic power. He suspended all foreign trade out of American ports, hoping that the loss of a crucial market would teach the belligerents a lesson and get the British and French to respect American vessels.

But Jefferson's trade embargo turned out to be a disaster, both economically and diplomatically. British and French traders easily evaded the restrictions, and other European merchants were able to "backfill" the business on the lucrative trade routes that American shippers had abandoned. Meanwhile, U.S. businesses lost their most valuable trading partners, New England fell into a depression, the Royal Navy continued to attack American sailors, and five years later, in 1812, the new United States was forced to declare war for the first time.

I mention this anecdote because it's a useful reminder of how much U.S. financial power has evolved since the early days of our Republic.

Compare, for example, Jefferson's failure to our ongoing efforts to use sanctions to prevent Iran from obtaining a nuclear weapon. Together with partners around the world, we have imposed what many believe is the most effective set of financial and economic sanctions in history. Carefully designed and customized to maximize pressure, they have impeded Iran's ability to acquire material for its nuclear program, isolated it from the international financial system, drastically slashed its oil exports, and deprived it of access to a sizeable portion of its oil revenues and foreign reserves.

Not surprisingly, the impact on Iran's economy has been dramatic: its budget deficit and inflation have spiked, the value of its currency has sharply declined, foreign investment has all but dried up, and overall economic activity has stagnated.

Most importantly, the sanctions advanced their fundamental policy goal: they helped bring the Iranians to the negotiating table, where they are seeking relief from the sanctions in exchange for taking steps that will ensure that they cannot produce a nuclear weapon.

As I'm sure you are all aware, the negotiation process is ongoing, as is the Joint Plan of Action, the understanding reached a little over a year ago between Iran and the P5+1 – that is, the United States, the United Kingdom, France, Germany, Russia and China. The JPOA halted progress on Iran's nuclear program, rolled it back in important respects, and provided unprecedented access to and inspections of Iran's enrichment facilities. In exchange, Iran received very modest and reversible relief from some nuclear-related sanctions. But the JPOA left in place the full architecture of our financial, banking, oil, and trade sanctions; our sanctions focused on Iran's support for terrorism and its violations of human rights; as well as our own domestic embargo.

Over the course of the JPOA, as the negotiations have proceeded – and as some important progress has been made – we have repeatedly reminded the world that Iran is not open for business. We have warned off countries and companies that are interested in doing still-sanctioned business with Iran, designated more than 90 individuals and entities that were helping Iran evade our sanctions, and imposed more than $350 million in penalties on those who have violated the sanctions.

Two weeks ago, the P5+1 agreed with Iran to extend the talks for another seven months total – four months to reach a framework understanding, and three additional months to work out the technical details. We agreed to extend the negotiations because, as I noted, our diplomatic teams have made progress. It also takes time to get to a good agreement, one that cuts off all of Iran's possible pathways to a nuclear weapon.

We may be able to reach a comprehensive deal; we may not. But there should be no doubt that the negotiations have made the world safer and put us in a stronger position to address this threat peacefully.

Over the next seven months, as the negotiations proceed, we will continue to take action against anyone, anywhere, who violates or attempts to violate our sanctions. We have the tools to continue to apply biting financial pressure on Iran without new nuclear-related sanctions legislation, which would likely have a negative effect on the prospects for a diplomatic solution. Put simply, the sanctions regime that helped bring Iran to the table remains in place, and so does our unflagging commitment to enforce it.

So why do targeted financial sanctions work, and why have they gotten better over time? I'd highlight a couple of reasons.

One reason is the United States' dedication – at home and abroad – to financial transparency. The success of our sanctions depends on the existence of a transparent, well-regulated financial system. By requiring the collection of key information regarding the nature of financial transactions, the parties that engage in them, and the individuals who ultimately stand to benefit from them, we have made it harder for illicit actors – states, terrorists, or criminals – to camouflage themselves in the legitimate economy. That's why financial transparency – building it, protecting it, and enforcing it – is at the core of Treasury's national security mission.

A second reason is structural. The U.S. Treasury's Office of Terrorism and Financial Intelligence – the Office I am proud to lead – is the only government agency anywhere that brings together under one roof the regulatory, policy, and enforcement expertise of a finance ministry with an in-house intelligence agency that delivers insights that only dedicated intelligence professionals can provide. The combination of an intimate familiarity with domestic and international financial markets, robust intelligence analysis, powerful regulatory and enforcement authorities, and the ability to communicate with both the private sector and international partners gives us a unique platform and perspective.

Technological innovation also has made it easier for both governments and financial institutions to track financial flows, screen for illicit transactions, and identify patterns of illicit behavior.

But there is a deeper story here. In recent decades, the preeminence of U.S. capital markets and the dollar's dominant role in global trade have put us in a powerful position to lead efforts to combat illicit finance. Put simply, financial institutions everywhere need dollars to serve their customers, and thus require access to U.S. banks through correspondent accounts to settle their customers' transactions. That means that foreign banks are especially attuned to our sanctions.

And particularly in the case of Iran, our ability to regulate access to the U.S. financial system has allowed us to present overseas financial institutions with a choice: play by the rules and continue to benefit from our financial system, or do business with sanctioned entities and be shut out. For most, this is an easy decision – one that amplifies our efforts to advance our national security.

We've also boosted the effectiveness of financial power through our increasingly close coordination with international partners, including with multilateral organizations like the EU and the UN. Our allies' willingness to implement robust sanctions measures of their own allows us to demand even greater vigilance from market participants.

Moreover, quite apart from the conditions that we, as regulators, can set for access to the U.S. financial system, the international financial system has grown more complex and interdependent, thereby increasing the costs for those unwilling to be responsible members of the international community. Modern transportation, trading, and telecommunications systems move people, goods, and money across borders at dizzying speeds. So the prospect of economic isolation serves as a powerful check on countries that hope to attract foreign investment and on banks and businesses that hope to prosper in a globalized world.

As a result of these trends, we have been able to move away from clunky and heavy-handed instruments of economic power. You don't have to think back to Jefferson; all of us in this room remember how sanctions used to consist primarily of trade restrictions or wholesale bans on commercial activity. With often high costs – on both the country sanctioning and the country being sanctioned – these embargoes rarely created meaningful pressure.

Sanctions that focus on bad actors within the financial sector are far more precise and far more effective than traditional trade sanctions. And the trade restrictions that we continue to employ today are also smarter and more surgical, targeting specific classes of products rather than cutting off entire economies.

The Innovative Nature of Russia Sanctions

The sanctions program we have developed over the past year in response to Russia's illegitimate and unlawful actions in Ukraine illustrates well the sophisticated and innovative nature of financial power today.

Since early this year, Russia has deliberately and brazenly worked to undermine the sovereignty and territorial integrity of Ukraine. President Putin's actions fly in the face of core international principles, chief among them that one nation cannot simply redraw borders by force.

The United States will not acquiesce to Russia's illegal occupation and attempted annexation of Crimea, nor to its continued support for separatists who, through violence, are challenging Ukraine's sovereignty in the country's Donbass region.

And so, beginning last March, President Obama issued three Executive Orders, which together give us broad authority to impose a range of sanctions on individuals and entities contributing to this conflict.

Let me be clear: None of our sanctions programs are intended as punishment, and the Russia sanctions program is no exception. These sanctions are intended to impede dangerous behavior and, above all, to influence Russian decision-making. Since the beginning of the crisis in Ukraine, it has been the Administration's goal to resolve this issue peacefully, in a way that respects Ukraine's sovereignty and is consistent with international law.

Our sanctions are one part of this strategy, and they have sharpened the choice for Russia. If it continues to support destabilizing activities in Ukraine, it will further isolate itself and incur increasing economic pain. But as President Obama and others have stressed repeatedly, Russia has an off-ramp. If Russia abides by international norms, including its commitments under the September Minsk Agreements, that would pave the way for its reintegration into the international community.

Now, from the start, we and our allies in Europe understood that imposing financial costs on Russia would require a creative approach. Russia's economy is far larger and more systemically important than that of any previous sanctions target. For the sake of comparison, the Russian economy is more than five times larger than the Iranian economy was in 2009, before the most powerful sanctions took effect, and Russia's major banks are far more integrated into the global financial system than Iran's ever were. So we needed a way to increase the pressure sufficiently to affect Moscow's calculations while minimizing the risk to global financial markets, global energy supplies, and overall economic activity in the United States and Europe.

To that end, our sanctions program contains several important innovations.

For starters, the measures we implemented are unusually precise and flexible – even more so than the targeted sanctions that we have developed over the past decade. Our so-called "sectoral" sanctions focus on specific critical aspects of the Russian economy – finance, energy, and defense – and then target specific entities in those sectors, most of which are state-owned and have close ties to, and influence in, the Kremlin. Exercising this authority, we have imposed sanctions on several important Russian banks, energy companies, and a large defense conglomerate.

Moreover, we have innovated in the type of sanctions we have imposed on those entities. In particular, we have devised restrictions that affect the long-term growth and investment plans of these targets while minimizing disruptions to the "plumbing" of the international financial system.

We did this by leveraging the key role of U.S. capital markets in international finance. Unlike most of our prior financial sanctions programs, we have neither blocked the assets of, nor prohibited transactions with, large Russian banks. Instead, we have limited the access of the six largest Russian state-owned financial institutions to our capital markets by prohibiting U.S. persons from dealing in any of the sanctioned banks' new equity issuances or new debt with maturities in excess of thirty days. The energy companies and the defense conglomerate face similar restrictions on their borrowing.

What this means is that, for all these firms, day-to-day operations can continue. But their ability to finance their long-term growth, which has historically required access to foreign capital, has been seriously hampered. As a result, the banks are struggling to refinance their debts and the energy firms are being forced to put off medium- and long-term, capital-intensive exploratory projects.

Meanwhile, the trade restrictions we have in place are also designed to impose costs in much more surgical ways than the broad embargoes of the past. For example, we know that the future of the Russian energy sector depends on developing shale, Arctic offshore, and deepwater oil deposits. But Russian firms cannot tap this oil without advanced U.S. and European technology and without the technical know-how of our energy services businesses. So together with our allies in Europe, our sanctions deny Russia what it needs to develop these resources.

Finally, these sanctions are an example of multilateral foreign policy at its best. In a global economy, a sanctions regime is far more powerful when a broad international coalition comes together – either under the umbrella of a UN Security Council resolution or, as in this case, on an ad hoc basis. It is also far preferable to act alongside others, because that way the economic burden of imposing sanctions is more widely, and more fairly, shared by those who benefit from efforts to confront, disrupt and deter threats to our collective security. That's why all the actions I outlined above have been carried out in close coordination with our EU and G-7 partners.

I know how important it is that U.S. and European sanctions line up closely. Some of you may represent clients that do business in both markets, and we want compliance to be as easy as it can be. And we also want there to be a level playing field for U.S. and European companies that do business in Russia. I can assure you that we are continuously working to close any gaps in our respective sanctions regimes and we value hearing from you on these issues.

One need only glance at the front page of the newspaper to see the effects our sanctions have had. The companies we have targeted are in a deep hole, and many of them have had to turn to the Russian state for assistance. Rosneft, for example, has asked for a $42 billion injection from the government to cover sanctions-related losses, and the Central Bank of Russia is being forced to draw on its foreign currency reserves to support the operations of some of the largest banks in the country.

On a macroeconomic level, the impacts are even starker, and they have been exacerbated by the decline in global oil prices. Until recently, the Russian government was predicting modest economic growth for next year. Now, for the first time in six years, it is forecasting a recession. The ruble has depreciated almost 40 percent since the beginning of the year and continues to lose value, despite the Central Bank's spending about $80 billion in an attempt to stabilize it. Borrowing costs and inflation are spiking, driving down consumption. And capital flight from Russia this year is expected to exceed $100 billion.

Now, the sanctions have not yet achieved our ultimate goal of bringing about a diplomatic resolution to the crisis in Ukraine. And we may never know what additional Russian aggression the sanctions, and the threat of additional sanctions, may have deterred. But there can be no doubt that we have created real costs for Russian firms and for the broader Russian economy – impacts that no leader can long ignore.

As President Obama has made clear, we are prepared to maintain this pressure – and increase it if necessary – until Russia respects its obligations and calm is restored in Ukraine.

Conclusion

Before closing, I'll tell a quick story. A few weeks ago I had occasion to speak with a representative from a U.S. company that does business in Russia. The sanctions have admittedly complicated matters for his company, and he described in detail the difficulties his company had encountered. But he said something else that stuck with me. Notwithstanding the impact on his business, he appreciated the need to impose costs in response to Moscow's recent behavior. He said, "If Russia were allowed to continue its actions unopposed, the situation might escalate even further, and at that point, doing business would be the least of any of our concerns."

His comments captured what is perhaps the most important use of our financial power. We deploy it not just to protect our own national security, but to preserve a broader world order and to uphold its core principles. Our targets are the aggressors, terrorists, criminals, and proliferators who threaten the international system that has delivered decades of rising peace and prosperity.

Financial power has become an essential component of our country's national security toolkit. That fact may mean that we are called on to use it more frequently and in more complex ways than we have in previous decades. And we understand that this creates new challenges for the private sector, particularly when it comes to compliance.

So my pledge to you is that when we deploy our financial power, we will remain absolutely transparent about what we are doing, why we are doing it, and how it may affect businesses here and around the world. We always want to hear from the private sector, and the feedback we get informs the work we do every day. You are on the frontlines in this effort, and without your partnership, diligence, and vigilance, we could not carry out our mission.

For that, and for your attention this afternoon, I thank you very much.

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