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"Implementing Tougher Sanctions on Iran: A Progress Report"

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Chairman Berman, Ranking Member Ros-Lehtinen, and distinguished members of the Committee, thank you for the opportunity to appear before you today to discuss the current status of the global effort to increase pressure on Iran. I am pleased to be here today with Under Secretary Bill Burns, who will explain the Administration's overall approach to Iran as well as the implementation of sanctions on the Iranian energy sector. I will provide you with an overview of the pressure strategy and recent actions taken by the U.S. and our international partners to hold Iran accountable for its continued illicit conduct as well as the critical role the Comprehensive Iran Sanctions, Accountability and Divestment Act of 2010 (CISADA) is already playing in our overall effectiveness. I will also describe the impact we have seen these measures having on Iran thus far.

While we still have a great deal of work in front of us, I can report today that we have made significant progress implementing our strategy. One key to our progress has been the impact of financial measures imposed by the U.S. and others in the wake of UNSCR 1929, including the financial provisions of CISADA. Today, Iran has dramatically reduced access to financial services from reputable banks, and is finding it increasingly difficult to conduct major transactions in dollars or euros. With great regularity, major companies are announcing that they have curtailed or completely pulled out of business dealings with Iran. And, as has been widely reported, Iran's leadership appears to have underestimated the severity and effects of the global financial measures, giving rise to internal Iranian criticism and finger pointing. The strategy is already beginning to have the effect it was designed to have: By sharpening the choice for Iran's leaders between integration with the international community and, alternatively, increasing isolation, we are creating the leverage needed for effective diplomacy.

Iran Sanctions Strategy

A little more than a year ago, I explained in testimony before Congress that we had developed a strategy to impose substantial costs on the government of Iran if and when the President determined that such pressure was needed to affect Iranian policies. The plan we developed took into account that no single sanction is a "silver bullet" and that we would need to impose a variety of measures simultaneously in order to increase their effectiveness. We also knew that we would need to target several of Iran's vulnerabilities simultaneously, and that we would need to secure the support of the largest possible international coalition of governments and private actors. Finally, because conduct-based financial measures that target illicit actors have proven to be an effective way to build such a broad coalition, we set out to focus our measures, to the extent possible, on Iran's illicit conduct, such as its proliferation of weapons of mass destruction (WMD) and support for terrorism.

By concentrating our sanctions programs on Iran's illicit conduct and its perpetrators – for example, the Islamic Revolutionary Guard Corps (IRGC) and Iran's national maritime carrier, the Islamic Republic of Iran Shipping Lines (IRISL) – we sought to maximize the chances of achieving a truly multinational coalition, because it is difficult for any government, whether an ally or not, to oppose taking action targeted against these types of activities. Equally as important, recognizing the commercial risks associated with doing business with Iran and to protect themselves from being unwitting participants in Iran's illicit conduct, private sector actors willingly implement the financial measures and, in fact, often take steps that go beyond the strict legal requirements. As more banks and businesses cut off their dealings with risky individuals and entities, the reputational risk increases for those that have not. This encourages additional firms to join in creating a ripple effect that amplifies the effect of sanctions. Moreover, when private sector consensus gels around taking certain actions, governments find it easier to require additional measures. The result is a mutually-reinforcing cycle of governmental and private sector action that isolates bad actors from the legitimate financial system. The effect of this on our targets is significant. When an individual or entity is cut off from access to international financial institutions, their ability to access the commercial sector is significantly affected.

As we designed our strategy, we also knew that Iran would seek to evade the measures we put in place. We therefore sought to create a sanctions program that is specifically adaptive and responsive to Iranian evasion attempts. The examples of Iran's deception are numerous. Iranian banks and companies have concealed their involvement in transactions by removing or stripping their names from transaction documents. Non-sanctioned Iranian banks have stepped into the shoes of sanctioned banks to disguise the role of sanctioned banks in transactions. IRISL, which we designated in 2008, has renamed and even repainted ships, and changed the nominal ownership of vessels, all to hide their connection to the shipping company. A good example of Iran's continued deceptive and illegal conduct has been widely reported recently. Just a few weeks ago, Nigeria intercepted and seized an Iranian weapons shipment, including 13 containers of rockets and explosives, which were labeled as building materials. Several Iranians in Nigeria quickly sought refuge in the Iranian embassy, and last week, a Nigerian court charged a reported member of the IRGC in the plot.

We have publicized this kind of deceptive activity and have taken enforcement action against those that have cooperated in these deceptive practices and thereby facilitated Iran's illicit conduct. Amid the wealth of derogatory information, the private sector has become increasingly wary of engaging in any business with Iran. Many in the private sector are simply unable to distinguish between Iran's legitimate and illicit transactions, and so they have opted to cut off Iran entirely. In this way, Iran's own evasion and deceptive conduct is further increasing its isolation.

UNSCR 1929 and its Implementation

It would be difficult to overstate the importance of UNSCR 1929 to our strategy. It has been essential to broadening our international coalition and is the foundation upon which robust sanctions implementation internationally has been based. In the diplomacy leading up to the adoption of UNSCR 1929, we pushed hard for provisions that would create this foundation.

UNSCR 1929 includes several significant provisions, including: A ban on certain ballistic missile activity; a ban on Iran's investment in nuclear and missile-related industries abroad; a ban on the export to Iran of certain heavy weapons; mechanisms for inspecting Iranian cargo and seizing contraband; and a requirement to exercise vigilance when conducting certain business with Iranian entities, including the IRGC and IRISL. On the financial side, UNSCR 1929 lays the foundation for robust international sanctions in its call to member states to prevent the provision of financial services (including banking, insurance, and reinsurance), if there are reasonable grounds to believe that such services *could* contribute to Iran's nuclear or missile programs. The vast body of public information demonstrating the scope of Iran's illicit conduct and deceptive practices — practices that have facilitated its proliferation activities — makes it nearly impossible for financial institutions and governments to assure themselves that transactions with Iran could not contribute to proliferation-sensitive activities.

Both prior to and in the aftermath of UNSCR 1929, we have worked closely with our allies to ensure serious and resolute follow-on implementation of its provisions. Over the past several months, the sanctions regimes adopted by the European Union, South Korea, Japan, Canada, Australia, Norway and others contain a number of powerful features. In addition to designating a wide range of actors engaged in illicit conduct, including the entire IRGC and IRISL, many of these sanctions programs also include: A prior authorization regime that requires the vetting of significant transactions with Iran; the imposition of severe restrictions on export credits for business with Iran; a prohibition — either formal or de facto — on the establishment of new branches of Iranian banks in these jurisdictions, or of their home-country banks in Iran; and formal or de facto prohibitions on the establishment of new correspondent relationships between their banks and Iranian banks.

In particular, the EU's regime exerted a great deal of influence over the shape of the sanctions programs enacted by other nations, for it contains a robust complement of systemic measures designed to protect against widespread Iranian abuse. The EU subjected scores of individuals and entities tied to Iran's nuclear, missile, and conventional weapons programs to an asset freeze – including Bank Mellat, Bank Saderat, Future Bank, Post Bank, Persia International Bank, the Export Development Bank of Iran – in addition to Bank Melli and Bank Sepah, which the EU had previously designated. The EU also designated the IRGC, IRISL, and numerous entities that are owned or controlled by, or operate on behalf of, those organizations. Significantly, the EU measures include an asset freeze on IRISL and a prohibition on the loading and unloading of cargoes on or from IRISL vessels in ports of EU Member States.

Beyond freezing the assets of a targeted list of individuals and entities, the EU's measures also comprehensively address the conduct of financial dealings with any Iranian person or entity. The EU's regime requires additional monitoring when doing any business with Iranian entities and entities owned or controlled by Iranian entities. In what is perhaps its most consequential measure, the EU has imposed a prior authorization regime designed with Iran's history of deceptive financial conduct in mind. Under the prior authorization regime, transactions to or from an Iranian individual or entity, of or above 40,000 Euros generally must be approved *in advance* by the EU host nation's regulator. Financial institutions must also notify their regulators of transactions to or from an Iranian individual or entity above 10,000 Euros. The EU also prohibited the provision of insurance and reinsurance to the Government of Iran or Iranian entities and banned the opening of new branches, subsidiaries, or representative offices of Iranian banks within the EU. Similarly, EU banks are prohibited from establishing new joint ventures or correspondent relationships with, or taking an ownership interest in, Iranian banks. They also are prohibited from opening new offices, subsidiaries, or banking accounts in Iran.

CISADA

When it passed CISADA, Congress took an extraordinarily effective step in bolstering U.S. sanctions authorities with respect to Iran. CISADA complements UNSCR 1929 and previously existing sanctions authorities by *inter alia* dramatically strengthening U.S. financial sanctions on Iran, restricting U.S. government contracts for companies that engage in sanctionable business with Iran, strengthening existing U.S. sanctions with respect to Iran's energy industry, and providing for sanctions on those responsible for or complicit in serious human rights abuses in Iran.

As you know, CISADA requires Treasury to issue regulations to prohibit or impose strict conditions on access to the U.S. financial system by any foreign financial institution that Treasury determines knowingly engages in one of the following activities: (1) facilitating the efforts of the Government of Iran (including the IRGC) to acquire or develop WMD or delivery systems for WMD, or to support terrorism; (2) facilitating the activities of a person subject to financial sanctions pursuant to UNSCRs with respect to Iran; (3) engaging in money laundering to carry out certain illicit conduct; (4) facilitating the efforts by the Central Bank of Iran or any other Iranian financial institution to engage in certain illicit conduct; or (5) facilitating significant business for U.S.-designated IRGC individuals or entities, or for financial institutions designated by the U.S. Government in connection with Iran's WMD program or support for international terrorism.

Treasury published the Iranian Financial Sanctions Regulations to give effect to the financial provisions of CISADA on August 16, 2010. The regulations implement these provisions in several ways, most importantly by describing the factors that Treasury may consider when determining whether to impose sanctions under CISADA. While any such determination will be made according to the totality of the facts and circumstances of each specific case, the factors we identify in the regulations that we may consider include the size, number, and frequency of the transactions; the level of awareness of the transactions by senior management and whether they are part of a pattern of conduct; and whether the financial services involve an attempt to engage in deceptive practices.

CISADA's financial provisions are quite powerful as they force a stark choice: If you conduct certain business with Iran, you risk losing access to the U.S. financial system. In this way, CISADA creates a multiplier effect for certain U.S. designations. Most notably, any significant business by a foreign financial institution with any U.S.-designated IRGC individual or entity or with any one of the 17 Iran-related financial institutions designated by the U.S. for terrorism or proliferation carries with it the possibility of that foreign financial institution being cut off from the U.S. financial system.

We have moved quickly to implement CISADA's financial provisions, and have already contacted governments and financial institutions in more than a dozen countries to investigate conduct that could be sanctionable under the Act. What we are seeing thus far is very positive – even banks that had been willing to maintain accounts for designated Iranian banks are now reversing course or cutting ties with Iran altogether. Nevertheless, we know that Iran continues to search for work-arounds, and we must and will remain vigilant in enforcing this law.

U.S. Actions and Outreach Help Drive Global Implementation of Sanctions

All elements of the Administration have been very active during the past several months in the implementation of U.S. and UN sanctions on Iran. Since the adoption of UNSCR 1929, Treasury has used its authorities to target the full range of Iran's illicit and deceptive conduct by imposing sanctions on illicit actors themselves, as well as the banks, front companies, and ships that are the conduits for their conduct. As part of a broader U.S. Government outreach effort, Treasury officials have also been traveling the world to encourage robust implementation of UNSCR 1929 and to educate other governments and the international private sector about recent U.S. measures, particularly CISADA.

Targeted Financial Measures

The actions taken since June generally fall into five categories: Iranian-owned banks; IRGC-affiliated targets; IRISL front companies and vessels; Iranian human rights violators; and Iranian government entities identified pursuant to the Iranian Transactions Regulations (ITR). In the category of actions against Iranian-owned banks, Treasury designated Iran's Post Bank shortly after the adoption of UNSCR 1929 for providing financial services to, and acting on behalf of, U.S.- and UN-designated Bank Sepah. Post Bank's history provides yet another example of the deceptive practices Iran routinely employs to evade sanctions. At one point, Post Bank's business was conducted almost entirely within Iran. With Iran's state-owned banks facing increasing sanctions, Iran began using Post Bank to facilitate international trade. Post Bank actively stepped into the shoes of Bank Sepah to carry out transactions set up by Bank Sepah and to hide Bank Sepah's involvement.

In September, Treasury also designated Iranian-owned Europäisch-Iranische Handelsbank (EIH), a bank located in Hamburg that had acted as a key financial lifeline for Iran and as one of Iran's few remaining access points to the European financial system. EIH had facilitated billions of dollars worth of transactions on behalf of Iranian banks previously designated for proliferation-related activities. EIH became the 17^{th} Iran-related bank designated in connection with Iran's provision of support to terrorism or its proliferation activities. As described above, because of the potential application of CISADA, these actions make it extraordinarily risky for any foreign financial institution to do business with EIH, Post Bank or any other Iranian banks we have designated.

Since June, Treasury has designated 10 IRGC-affiliated individuals and entities for facilitating Iran's nuclear and ballistic missile program or support for terrorism. First designated by the U.S. in 2007, the IRGC is the epitome of a conduct-based sanctions target because of its range of illicit conduct – its support for terrorism, its involvement in Iran's proliferation activities, and its suppression of domestic dissent, including in the aftermath of the June 2009 election. Since June we have also exposed and designated 53 IRISL front companies, 9 IRISL officials, identified 27 vessels as property blocked because of their connection to IRISL, and updated the entries for 71 already-blocked IRISL vessels to identify new names given to these vessels as part of IRISL's efforts to evade sanctions.

In September, President Obama signed an Executive Order that imposes sanctions on Iranian officials determined to be responsible for or complicit in, the commission of serious human rights abuses involving Iran. In signing the Order, the President identified for sanctions eight Iranian individuals who share responsibility for serious violation of human rights that have occurred since the June 2009 disputed presidential election. Among those identified were IRGC officials and Iranian government ministers.

Since June, we have also identified, pursuant to the ITR, 43 entities in the banking, investment, mining, engineering, insurance, energy, petroleum, and petrochemical industries determined to be the Government of Iran. Many of these entities are located outside of Iran and have names that make it difficult to recognize them as Iranian government entities. By listing these entities pursuant to the ITR, we both help U.S. persons comply with U.S. law prohibiting business with Iranian government entities and also assist private sector actors around the world that are increasingly deciding to shun business with the government of Iran.

Global Engagement

As I noted earlier, since the adoption of UNSCR 1929, Treasury has continued its campaign of engagement regarding Iran’s illicit conduct. Over the last several months, my colleagues and I have traveled around the world to speak to governments and private sector representatives about Iran sanctions issues, including CISADA. By the end of this week, we will have visited 24 countries – Belgium, Denmark, France, Germany, Switzerland, the Netherlands, Brazil, Ecuador, Japan, China, South Korea, Armenia, Azerbaijan, Georgia, Pakistan, Lebanon, Turkey, Iraq, Kuwait, Bahrain, Oman, Qatar, Saudi Arabia, and the United Arab Emirates – to discuss the risks posed by Iranian financial activity and the steps necessary to control those risks.

In particular, we have worked with our partners as they shape their own implementation of UNSCR 1929 and we have sought to educate both governments and the private sector – including scores of foreign banks – on CISADA. CISADA is a powerful tool and we do not want international financial institutions to be surprised by the potential consequences that flow from it. The responses we have received from foreign regulators and financial institutions in the course of this outreach have been overwhelmingly positive, and it is clear that the provisions of UNSCR 1929 and CISADA are being taken seriously.

The Impact of Sanctions

In the course of our travels, we have encountered a growing number of financial institutions, driven by increased awareness of Iran’s illicit and deceptive conduct, that are shying away from doing any kind of business with Iran. Many institutions have simply stopped dealing with

Iranian banks altogether, in light of Iran's established history of using deceptive financial practices to mask the real nature of, or the true parties involved in, their transactions.

As a direct result, Iran has become increasingly isolated from the international financial system, with limited access to financial services. And, without access to financial services, it becomes difficult to conduct commercial transactions of all kinds. Just a few years ago, Iran was able to access financial services from the world's largest and most prestigious financial institutions. Today, by contrast, Iran has been relegated to the margins of the international financial system, and is finding it increasingly difficult to access the large-scale, sophisticated financial services necessary to run a modern economy efficiently.

The movement away from business with Iran has not been restricted to the financial services sector. Companies from many industries, including manufacturing, automobile, insurance, engineering, and accounting, have similarly announced the withdrawal of business from Iran. Many foreign energy companies have also withdrawn their investments in Iranian petroleum projects, and have pulled out of joint ventures with Iranian energy companies. Some European and Middle Eastern companies have even stopped providing jet fuel to Iran's national air carrier in Europe. Iran is finding it more difficult to import refined petroleum products and is being forced to make tough domestic trade-offs to fill the gap. And Iran is increasingly unable to secure the foreign investment, financing, and technology it needs to modernize its aging energy infrastructure, threatening its oil and gas production and export capacity over the long term. The Iranian economy depends on energy revenues, and the continued stagnation, or decline, of energy outputs will adversely affect Iran's economic stability.

The Iranian leadership's inability to develop its most important industry could have long-term political as well as economic consequences as Iran struggles to create jobs for its disproportionately young population. Unemployment is currently 12 percent, even according to unreliable official estimates; Iran's parliament has claimed that it is as high as 22 percent. People under age 30 account for three out of four unemployed Iranians.

The degradation of Iran's access to the international financial system has also made it very difficult for Iran to make payments on loans and maintain insurance coverage on IRISL ships, which is having an impact on the shipping company's ability to continue operations. Just a few months ago, Credit Agricole Corporate & Investment Bank seized three IRISL ships in Singapore to recover $110 million on a $235 million loan arranged in 2006 to finance ships ordered by IRISL. According to news reports, the bank claimed that IRISL breached its loan covenants, particularly its obligation to maintain insurance.

Iran is poorly positioned to respond to the impact of sanctions and, as the leadership tries to formulate a response, it is faced with unappealing choices. As an example, in part because it is encountering difficulties in acquiring refined gasoline because of sanctions, the government is seeking ways to reduce domestic demand for gasoline. One obvious step would be to reduce the heavy subsidies on gasoline that now make the price at the pump about 37 cents per gallon. Iran recently announced that it would reduce subsidies on gasoline and other household and energy products by $20 billion. The government, however, has hesitated to go forward with these subsidy cuts most likely because of concern about popular backlash. They have even deployed security forces to try to enforce order and President Ahmadinejad has even threatened to severely punish businesses that raise prices of consumer goods in reaction to subsidy cuts. Additionally, fears that inflation could accelerate surrounding government implementation of subsidy reform, combined with increased barriers to Iranian banks and currency exchanges accessing dollars as a result of the implementation of recent sanctions, were likely the cause of the sudden near-20% depreciation of the Iranian rial on market exchanges in late September. The Central Bank of Iran was slow to respond to these pressures, and it took weeks of intervention to stabilize volatility in the rial market exchange rate.

Because of consistent pressure from sanctions over recent years and difficulties in attracting foreign sources of investment, the Iranian government is increasingly turning to the IRGC to maintain its hold on political power and for key economic projects. The Iranian government has turned over to the IRGC major transportation and energy sector projects, including the development of oil and gas fields. Indeed, the IRGC is taking increasing control over significant portions of the Iranian economy, and it is doing so with the help of sole-source contracts that deprive average Iranians of economic opportunity.

The IRGC itself is, of course, a key target of U.S. and international sanctions, which means that Iranian government reliance on the IRGC will only deepen Iran's isolation. For example, because Iran could not attract a suitable foreign energy firm to develop phases of the South Pars gas field, Iran gave the opportunity to Khatam al-Anbiya, an IRGC-controlled company. However, Khatam al-Anbiya lacked the capability to develop the project itself. Because of its inability to develop this project without foreign partners, Khatam al-Anbiya was forced to withdraw from the project following designations by the U.S., then the EU, and finally by the UN. Using the IRGC to fill its investment gap will thus only make matters worse for Iran. The UN Security Council has now designated most of the major companies controlled by the IRGC and many of its senior officers for proliferation, and the EU, Japan, South Korea, and of course the United States, have also designated the IRGC in its entirety. The example of Khatam al-Anbiya is representative of our conduct-based strategy at work: As Iran is forced to rely on entities that have been exposed for bad conduct, it will find its options increasingly limited and will have greater difficulty coping with sanctions.

We believe that the speed, scope, and impact of sanctions have caught the regime by surprise. There are clear signs that the Iranian leadership is worried about the impact of these measures and is taking sanctions seriously. Earlier this fall, a high-ranking Iranian official warned against dismissing international sanctions as a "joke," saying the Islamic republic was facing its worst ever "assault" from the global community. As the pressure on Iran has increased, so has internal criticism and questioning of President Ahmadinejad and others for their handling of Iran's response to sanctions.

Conclusion

As a result of the international community's recent sanctions measures, including CISADA, and of our efforts to publicize Iran's illicit and deceptive conduct, Iran is feeling the pressure of sanctions as never before. Iran is struggling to find access to the international financial system, without which it is difficult to run an economy on the scale that a country like Iran needs.

While we believe that sanctions are having a real impact, we are also confident that Iran will continue to engage in illicit activity, and to employ deceptive conduct to mask that activity and otherwise evade sanctions. The examples I discussed earlier of Post Bank, IRISL, and the weapons shipment seized by Nigeria are only three examples of Iran's well-established practice of trying to evade sanctions. While our strategy was designed to account for Iran's attempts at evasion and we have been aggressive in highlighting and stopping such activities, we cannot afford to let up. In September, a high-ranking Iranian government official underscored exactly the effect we have tried to create when he said that "we have never had such intensified sanctions and they are getting more intensified every day. Whenever we find a loophole, they block it." In order to maintain this atmosphere, we must continue to actively seek out, publicly expose, and shut down Iran's efforts at evasion. We must also try to use Iran's deception to our advantage to forge an ever-more determined coalition to curtail Iran's illicit conduct.

In order to maintain and even increase the impact we have created so far, we need to remain vigilant and intensify our efforts. By doing so, we can continue to create the leverage needed for our diplomacy to be effective. I look forward to continuing our work with this Committee to achieve that goal.