The Honorable David S. Cohen
U.S. Department of the Treasury

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INTRODUCTION

Chairman Kerry, Ranking Member Lugar, and distinguished members of the Committee: Thank you for the opportunity to appear before you today, along with my friend and colleague Under Secretary Sherman, to discuss the Department of the Treasury's contribution to the Obama Administration's integrated strategy to address the threat posed by Iran's nuclear activities and its extensive support for terrorism.

I will focus my remarks today on our Iran sanctions strategy, with particular emphasis on the Treasury Department's most recent action to expose the extensive illicit finance threat that the entire Iranian financial sector—including Iran's Central Bank—poses to the international financial system. I will also discuss the impact that our implementation of the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA) and other financial sanctions are having on Iran, as well as our plans to increase the cost of Iran's intransigence until Iran agrees to curtail its pursuit of nuclear weapons. As I will explain, we are at a critical crossroad today in our effort to bring consequential pressure to bear on Iran. The options that we are now considering, including additional sanctions against the CBI, require that we work together to ensure that we deliver strong and well-targeted pressure on Iran.

Iran Sanctions Strategy

The Treasury Department's increasingly powerful and disruptive sanctions are embedded in the dual-track strategy that the United States and our allies are pursuing to address Iran's continued failure to meet its international obligations regarding its nuclear program. As Under Secretary Sherman describes in her testimony, the Obama Administration has presented Iran with a genuine opportunity for dialogue, creating a clear choice for Tehran. Iran's leadership can choose to meet Iran's international obligations, allowing Iran to deepen its economic and political integration with the world and achieve greater security and prosperity for the Iranian people. Or, Tehran can continue to flout its responsibilities and face even greater pressure and isolation. Unfortunately, Iran has steadfastly refused to respond meaningfully to the Administration's offer of engagement and has continued to pursue technologies and equipment that could only be applied to a nuclear weapons program. Just last month, the International Atomic Energy Agency (IAEA) issued a stark report laying out in detail Iran's past and present nuclear weapons-related activities. Shortly thereafter, the IAEA's Board of Governors adopted a resolution expressing its "deep and increasing concern" about unresolved questions regarding Iran's nuclear program, including its possible military dimensions.

Our broad-based pressure strategy is aimed at persuading Iran to change its course and to make clear to Iran the consequences of its continued intransigent behavior. Among the most important elements of this strategy are targeted financial measures designed to disrupt Iran's illicit activity and to protect the international financial system from Iran's abuse. We have focused our efforts on exposing Iranian entities' illicit and deceptive activities, an approach that has garnered support among foreign governments and led them to take similar actions, enhancing substantially the impact of our actions. Because these actions have highlighted the pervasive nature of Iran's illicit and deceptive conduct and the reputational risks associated with Iran-related business, the private sector around the world has taken notice and has often taken voluntary steps beyond their strict legal obligations, further amplifying government actions.

Our ability to implement this pressure strategy was strengthened considerably last year when President Obama signed CISADA into law. CISADA has helped us make the case to foreign governments and foreign financial institutions that neither the Islamic Revolutionary Guard Corps (IRGC) nor Iranian banks designated for their involvement in support for proliferation and terrorism should be allowed to have access to the international financial system. The results have been dramatic: our implementation of CISADA has resulted in a massive disruption of designated Iranian banks' access to the international financial system, impeding their ability to facilitate Iran's illicit activities and creating unprecedented financial and commercial isolation for Iran.

Implementing the Pressure Strategy

In implementing the pressure strategy, Treasury has focused on developing sanctions actions that expose the Iranian government's involvement in a broad range of illicit conduct, including nuclear and missile proliferation, support for terrorism, human rights abuses, and deceptive financial conduct and evasion of international sanctions. Our actions in recent months illustrate that such illicit conduct is indeed pervasive in multiple Iranian government sectors – including Iran's government-owned banks, its government-operated transportation infrastructure, and the IRGC, a branch of Iran's military. Examples of recent actions targeting Iranian illicit conduct include:

- **Abuse of the Global Financial System**. Treasury actions targeting Iranian banks are intended to prevent those banks from using the international financial system to facilitate Iran's proliferation activity or terrorism support, or from assisting other banks or entities in evading U.S. or international sanctions. We continued these efforts in May by designating Iran's **Bank of Industry and Mine** (BIM) under E.O. 13382 for providing financial services for other designated Iranian banks. BIM is the 22nd Iranian-state owned financial institution to be designated by Treasury in the last five years.

- **Use of Transportation Infrastructure to Facilitate Illicit Conduct**. Our actions against key elements of Iran's transportation infrastructure are aimed at impeding Iran's use of ships, airlines and ports for its proliferation-related or terrorism support activities. This year, we designated **Tidewater Middle East Co. (Tidewater)**, an IRGC-owned port operating company that manages the main container terminal at Bandar Abbas and has operations at six other Iranian ports. We imposed sanctions against **Iran Air**, the Iranian national airline carrier and its largest airline, because it has been used by the IRGC and Iran's Ministry of Defense for Armed Forces Logistics (MODAFL) to transport military-related equipment. We also designated the second largest airline in Iran, Iranian commercial airline **Mahan Air,** for providing financial, material, and technological support to the IRGC-Qods Force. We sanctioned 46 companies and individuals affiliated with Iran's national maritime carrier, the **Islamic Republic of Iran Shipping Lines,** which is subject to U.S. and international sanctions, and three individuals who each play a key role in aiding IRISL's sanctions evasion activities worldwide.

- **Human Rights Abuses.** As the Iranian regime's abuse of its citizens' human rights has continued, Treasury, working with State, has imposed sanctions against **11 senior Iranian officials** and **three Iranian entities—the IRGC, the Basij Resistance Force, and Iran's Law Enforcement Forces (LEF)—**including the IRGC's commander, the LEF chief, and Iran's Intelligence Minister. Under an authority that targets those responsible for or complicit in human rights abuses in Syria, Treasury designated the LEF for supporting the Syrian General Intelligence Directorate in its brutal suppression of the Syrian people. Treasury also designated LEF's Chief and Deputy Chief, and two senior IRGC-Qods Force officers, including IRGC-QF Commander Qasem Soleimani for supporting the brutal suppression of the Syrian people orchestrated by the Syrian General Intelligence Directorate.

- **Support for Terrorism.** We designated **six members of an al-Qa'ida facilitation network** operating in Iran under an agreement with the Iranian government, thereby degrading this network's ability to function while exposing Iran's continued support for terrorism worldwide. Treasury also sanctioned **five individuals,** including four senior IRGC-QF officers – among them the previously designated IRGC-QF Commander Soleimani -- connected to a plot to assassinate the Saudi Arabian Ambassador to the United States Adel Al-Jubeir and carry out follow-on attacks against other countries' interests inside the United States and in another country.

- **Proliferation-related Activities:** On November 21, the State Department and Treasury designated **10 entities and one individual** for their links to the Atomic Energy Organization of Iran (AEOI), the main Iranian organization responsible for research and development activities in the field of nuclear technology, including Iran's centrifuge enrichment program and experimental laser enrichment of uranium program.

Exposing the Iranian Financial Sector as an Illicit Finance Risk

The depth and breadth of Iranian financial institutions' illicit activities—from direct support for proliferation transactions, to assisting known proliferators' sanctions evasion efforts, to operating without appropriate regulatory controls—means that any financial institution that transacts with any Iranian bank runs a grave risk of facilitating Iran's illicit activities. Recognizing this pervasive risk to the U.S. and international financial systems, Treasury took regulatory action on November 21 to identify the *entire* Iranian financial sector—including not only already designated banks and their branches operating outside of Iran, but also non-designated banks, their foreign affiliates, and the Central Bank of Iran (CBI)–for posing an illicit finance risk to the global financial system. We did so by identifying Iran as a jurisdiction of "primary money laundering concern" pursuant to Section 311 of the USA PATRIOT Act.

The term "primary money laundering concern" covers multiple forms of illicit finance of greatest concern, such as terrorist financing and WMD proliferation financing. Indeed, the Section 311 finding against Iran sets out an unambiguous public record of the broad scope of Iran's illicit conduct. In particular, the finding describes Iran's activities as a state sponsor of terrorism, its longstanding provision of financing and support to Hizballah, Hamas, and other terrorist organizations, and more recent Iranian cooperation with al-Qa'ida. The finding explains the role that the IRGC and the IRGC-Qods Force, in particular, play in facilitating Iran's support for terrorism. The Qods Force involvement in terrorism support has been highlighted most recently in the public allegations that the Qods Force was involved in an Iranian plot to assassinate the Saudi ambassador to the United States. The finding also explains Iran's use of its banks, such as Bank Saderat, to provide terrorist financing, and describes its lack of sufficient laws to combat terrorist financing.

In addition, the finding makes a full case with respect to Iranian financial sector involvement in the financing of WMD proliferation, providing a detailed accounting of the many banks in Iran that engage in such activity. The finding explains the deceptive financial practices that Iranian banks use to disguise illicit conduct, and explains the role that exchange houses and front companies play in this deception, and Iran's involvement in the stripping of identifying information off of international wire transfers, putting the foreign banks that handle such transfers at risk for involvement in illicit conduct.

The Section 311 finding also provides new information about the role of Iran's Central Bank in facilitating illicit conduct and sanctions evasion. Since Section 311 was enacted in 2001, Treasury has applied it on a few occasions to other jurisdictions that pose substantial money laundering threats. But in each prior instance where special measures were proposed, Treasury explicitly exempted central banks from the reach of the so-called "jurisdiction 311" in order to allow the central bank to perform those duties that central banks customarily execute.

Not so this time, and for good reason. Iran presents a unique case. As the November 21 finding explains, the Central Bank of Iran is actively facilitating the evasion of international sanctions by supporting Iran's designated banks. For example, the CBI assisted designated Iranian banks, including Bank Saderat, Bank Mellat, the Export Development Bank of Iran, and Bank Melli, by transferring billions of dollars to them through a variety of payment schemes designed to deceive large international banks and take advantage of smaller, perhaps less sophisticated intermediaries. Similarly, the CBI also provided financial support directly to the U.S.-, EU-, and UNSC-designated engineering arm of the IRGC, Khatam al-Anbiya, which has been involved in Iran's proliferation activities and has been recruited to develop Iran's key energy resources.

This regulatory action reinforces U.S. and international sanctions already in place against Iran and provides greater certainty that the U.S. financial system is protected from Iranian illicit activity. While U.S. financial institutions already are generally prohibited from engaging in both direct and indirect transfers with Iranian financial institutions, Treasury's Financial Crimes Enforcement Network (FinCEN) issued a proposed rule alongside the 311 finding that would require U.S. financial institutions to implement additional due diligence measures in order to prevent any improper indirect access by Iranian banking institutions to U.S. correspondent accounts. Although the Section 311 action will have a regulatory impact for U.S. banks, we also expect that it will have a broader chilling effect on foreign banks' willingness to do business with Iran, given the risks that are detailed in the finding.

The U.S. is by no means alone in its assessment of the risks posed by the Iranian financial system. The UK and Canada also took similar strong actions on November 21 to protect their respective financial sectors from the Iranian threat. Highlighting that "the Iranian regime's actions pose a significant threat to the UK's national security and the international community," the UK announced that it had imposed new financial restrictions against Iran by cutting off Iran's banking sector from access to the UK. All UK credit and financial institutions are now generally required to cease business relationships and transactions with all Iranian banks, including the Central Bank of Iran, and their branches and subsidiaries. For its part, Canada imposed new restrictions under its Special Economic Measures Act in response to the IAEA's report, prohibiting financial transactions with Iran, sanctioning additional individuals and entities, and expanding the list of prohibited goods.

U.S., UK and Canadian concerns about the risks posed by the Iranian financial system are only further reinforced by recent reports of a massive embezzlement scandal in Iran. The Government of Iran has accused a network of Iranian state-owned and private banks of forging documents and issuing fictitious and fraudulent loans with an estimated value of approximately $2.6 billion to politically-connected individuals for the purchase of stakes in state-owned companies. The scandal has thrown into sharp relief the Iranian government's abiding weakness in the supervision of its financial sector and echoes the extensive fraud and corruption that exists in many sectors of the Iranian economy. While the regime has tried to distance itself from the scandal as much as possible, the Minister of Economy and Finance, Shamseddin Hosseini, who narrowly survived an impeachment vote by the Iranian Parliament, has publicly conceded that "we need to have a multi-level oversight system so institutions can control the loans they disburse," acknowledging that had such safeguards been in place, "such a huge fraud could not have happened in the banking system."[1] The scandal, implicating the highest levels of the Iranian government, including the Deputy Governor of the CBI, reinforces persistent doubts about the integrity of Iran's financial sector.

The Impact of Sanctions on Iran's Financial Sector

During testimony before the Senate Banking Committee in October, I reported that Iran's financial isolation, and the economic impact of that isolation, have continued to grow. Today, I can report that the trend continues to accelerate.

Due to a combination of factors—including UNSCR 1929, financial sanctions imposed by the U.S., EU, and other like-minded countries, and foreign banks' interest in avoiding CISADA actions or the reputational risk of doing business with Iran—the number and quality of foreign banks willing to transact with designated Iranian financial institutions has dropped precipitously

[1] "Heads of Three Government Branches Recount Positions on Bank Corruption Case," Tehran Donya-ye Eqtesad Online, November 9, 2011.

over the last year. Today, Iran's largest state-owned banks—each of which has been sanctioned by the U.S., the EU, and several of our allies—are largely unable to access the international financial system. Iran's shrinking access to financial services and trade finance has made it more difficult for Iran to attract foreign investment, pay for imports, and receive payment for exports. This has exacerbated persistent macroeconomic weakness due to the Iranian government's mismanagement of its economy.

One good illustration of the economic pressure resulting from this financial squeeze is Iran's recent difficulty in defending the value of its currency, the rial. For nearly a decade, the CBI has supported a single, official exchange rate for the rial, using hard currency earned through oil sales to stabilize it. Since the adoption of UNSCR 1929 and various UN member states' actions to implement the Resolution, however, the CBI has struggled to maintain stability in Iran's currency markets. Sanctions have increased the cost and difficulty of accessing adequate foreign exchange, weakening the CBI's ability to respond adequately to pressures in currency markets, particularly as accelerating inflation has exerted unusual pressure on the rial exchange rate. This has produced a multiple-tier currency market in Iran— including an official exchange rate and an even-more-expensive market rate.

In September 2010, the spread between the official and the market exchange rate widened dramatically. While the rial made a moderate recovery during the Fall of 2010, it rapidly began to lose value again in January 2011. To close this gap, the CBI devaluated the rial by 11 percent in June 2011. The CBI's policy response, however, failed to stabilize the market, and the rial plunged in value against the dollar and the euro over the past several weeks.

Today, the spread between the official and open market rates hovers above 20 percent, one of the highest levels in recent history, fueling serious inflation, high unemployment, and domestic discontent. (A chart depicting the increasing spread between the official and market rate is appended to my testimony.) Because of the rial's decline in value, ordinary Iranians are urgently seeking out foreign currency, such as dollars or Euros, for safety, yet they are having trouble accessing hard currency, and when they can, they have to pay the unofficial market rate. At the same time, senior government officials and preferred businesses, including IRGC-owned and controlled operations, are able to access foreign exchange at the official rate, essentially engaging in profitable arbitrage on the back of the average Iranian. Central Bank Governor Bahmani has conceded that the CBI has limited ability to respond to volatility in currency markets and blamed U.S. and international sanctions, noting that "Iran is now facing international restrictions and this has to be taken into consideration."[2] Iran's ability to respond to macroeconomic challenges will continue to be hampered by sanctions, at great cost to Iran's long-term economic growth.

There is little doubt that our sanctions strategy has markedly reduced Iran's access to the international financial system and, consequently, has contributed to a noticeable weakening of the Iranian economy. In a recent speech to the Iranian Parliament, President Ahmadinejad finally admitted the strong impact that sanctions are having on Iran's economy. He noted that "the West imposed the most extensive… sanctions ever" and that "this is the heaviest economic

[2] "Heads of Three Government Branches Recount Positions on Bank Corruption Case," Tehran Donya-ye Eqtesad Online, November 9, 2011.

onslaught on a nation in history." He went on to acknowledge that "every day, all our banking and trade activities and our agreements are being monitored and blocked."[3] This significant admission is a clear sign that U.S. and international sanctions are having a strong impact on the Iranian economy and the Iranian regime.

The Continuing Threat and the Way Forward

In light of the mounting evidence of the impact of sanctions, and in light of Iran's continued refusal to engage meaningfully and substantively with the international community, we are committed to applying greater financial and economic pressure on Iran. Let me be clear: We are firmly devoted to significantly intensifying the pressure on Iran, and doing so in a way that delivers swift, focused and powerful pressure on the Iranian leadership to further sharpen their choice between isolation and engagement.

As we explore opportunities to increase pressure on Iran, we are keenly focused—as is the Congress—on applying additional sanctions on the Central Bank of Iran. So we welcome French President Sarkozy's suggestion last week for a multilateral asset freeze on the CBI, as we recognize that coordinated and focused action against the CBI could have a particularly powerful impact on Iran's access to the international financial system and its ability to access the hard currency it earns from oil sales. And we welcome the opportunity to continue to work with Congress on an effective, well-designed and well-targeted sanction against the CBI. As we prepare these steps, it is imperative that we act in a way that does not threaten to fracture the international coalition of nations committed to the dual-track approach, does not inadvertently redound to Iran's economic benefit, and brings real and meaningful pressure to bear on Iran.

It is also important to remember that delivering potent pressure on Iran is not wholly dependent on how we address the Central Bank. Put simply, a designation of the CBI is not the only step, nor would it be the last step, available to bring consequential pressure to bear on Iran. For example, as more and more countries and foreign banks refuse to deal with designated Iranian banks, we remain keenly focused on the possibility that non-designated Iranian financial institutions may become involved in proliferation activity or terrorist financing. When we see Iranian banks stepping in to pick up business for designated banks, or beginning to process proliferation transactions, we will swiftly impose new sanctions, as was the case recently with Bank of Industry and Mine.

We will continue our intensive efforts to implement CISADA, which, as I noted, have been enormously successful in driving down to almost nil the international activity of designated Iranian banks. As we learn of activities that may trigger CISADA sanctions, we will continue to either obtain immediate resolution or impose CISADA sanctions.

We will stay ahead of efforts by Iran to develop workarounds to its financial isolation. This means working with our partners around the world to identify the ways—both overt and deceptive—in which Iran seeks to establish new financial footholds, and take action to stop them.

[3] "Ahmadinejad Stresses System Unity at Minister's Impeachment Hearing," Tehran Voice of the Islamic Republic of Iran, November 1, 2011.

We will relentlessly pursue IRISL ships, front companies, agents and managers, exposing and sanctioning them, and driving IRISL out of operation. And, as evidenced by the Tidewater designation in June, we will aggressively expose the IRGC's expanding role in the Iranian economy and work with our partners in Europe and elsewhere to apply sanctions on IRGC-controlled companies.

Conclusion

Although we are making progress to identify Iran's illicit behavior and pressure Iran to comply with its international obligations, there is, of course, significant work still before us. The recent IAEA report, which exposes Iran's activities relevant to the development of a nuclear explosive device, coupled with the recently exposed plot by which Iran's IRGC-QF planned to assassinate the Saudi Ambassador to the United States, only underscores the importance of not only maintaining, but qualitatively enhancing, the pressure on Iran.

As Secretary Geithner has said, "the policies that Iran is pursuing are unacceptable – and until Iran's leadership agrees to abandon this dangerous course, we will continue to use tough and innovative means to impose severe economic and financial consequences on Iran's leadership." We want to work with Congress to broaden and strengthen CISADA and other Treasury authorities and to take careful, focused steps to address the illicit conduct of the CBI.
I look forward to continuing our work with this Committee as Treasury continues to pursue this enormously important strategic objective.

APPENDIX: IRANIAN RIAL EXCHANGE RATE