



## **DEPARTMENT OF THE TREASURY OFFICE OF PUBLIC AFFAIRS**

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### **TESTIMONY OF STUART LEVEY UNDER SECRETARY FOR TERRORISM AND FINANCIAL INTELLIGENCE BEFORE THE SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS**

**WASHINGTON, DC-** Chairman Dodd, Ranking Member Shelby and distinguished members of the Committee, thank you for the opportunity to speak with you today about the Treasury Department's role in dealing with the myriad challenges posed by the radical regime in Iran. I welcome this Committee's ongoing focus on the Iranian threat, and, more broadly, your continued support for our efforts to stop illicit financial flows.

#### **INTRODUCTION**

The challenges posed by Iran have become particularly urgent, and the Administration is employing a multi-faceted strategy to meet them. I know you are hearing much about that strategy today from my colleague, Under Secretary of State for Political Affairs Nicholas Burns. The Department of State's diplomatic efforts have yielded critical successes, including a unanimously adopted UN Security Council resolution last December, Resolution 1737, imposing Chapter CII sanctions on Iran's nuclear and missile programs. As a result of Iran's noncompliance with that resolution, including its expansion rather than suspension, of uranium enrichment, the Security Council is now set to pass a follow-on resolution with expanded sanctions. That our international partners now support pressuring the Iranian regime to comply with its international obligations is a true credit to Under Secretary Burns's patient, yet persistent, diplomacy.

The Treasury developed the financial component of the Administration's overall Iran strategy at the direction of Secretary Rice and Secretary Paulson and in close coordination with other agencies. Through our teamwork, we have crafted an innovative strategy to highlight the reckless and dangerous conduct of the Iranian regime, deter Tehran's dangerous activities through the use of financial measures, and prevent the regime's abuse and manipulation of the international financial system. As I will discuss, the Treasury's efforts and the State Department's intensive diplomacy at the United Nations are mutually reinforcing.

Over the past nine months, senior Treasury Department officials, including Secretary Paulson and Deputy Secretary Kimmitt, have met with foreign finance ministry and central bank counterparts from tens of countries -- in many cases multiple times -- to discuss the imperative of ensuring that the international financial system is not tainted or harmed by Iran's abuse. We have also 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. And we have implemented targeted financial measures against Iranian banks, entities, and individuals engaged in illicit activities, highlighting to the world their dangerous conduct, preventing U.S. persons from doing any business with them, and, in some cases, requiring that any assets subject to U.S. jurisdiction be frozen. Those targeted actions have helped pave the way for international action.

Today, I would like to give you an overview of these Treasury efforts.

#### IRANIAN THREAT AND DECEPTION

Mr. Chairman, the Committee is well aware of the threat posed by Iran's dangerous activities, so I will just briefly summarize the problem. Iran poses two threats -- an unrelenting pursuit of a nuclear weapons capability, on the one hand, and the provision of financial and material support to terrorist groups, on the other -- the combination of which has an extraordinarily lethal potential. Under President Ahmadinejad, the regime has ignored calls from the International Atomic Energy Agency (IAEA) and the UN Security Council to suspend its enrichment-related and reprocessing activities, and to comply with its obligations under the Non-Proliferation Treaty. The danger we face is that Ahmadinejad not only has an extreme vision of the future but that he might develop the weapons that make him believe that his vision can be obtained.

Iran's role in supporting international terrorism is of serious concern. Iran has long been a state sponsor of terrorism. Tehran arms, funds, and advises Hizballah, an organization that has killed more Americans than any terrorist network except for al Qaeda. It is also widely reported that Iran provides extensive support to Palestinian terrorist organizations, including the Palestinian Islamic Jihad (PIJ) and Hamas. In the case of PIJ, Iran's financial support has been contingent upon the terrorist group carrying out attacks against Israel. And we are all familiar with Iran's funding and equipping of elements of the insurgency in Iraq, further destabilizing that country and resulting in deaths of Americans, Iraqis and others. Iran needs money to provide all of this support. Indeed, the regime operates as the central banker of terror, spending hundreds of millions of dollars each year to fund terrorism.

Iran also uses its Islamic Revolutionary Guard Corps, or IRGC, to provide a 'train and equip program' for terrorist organizations like Hizballah, as well as to pursue other military objectives of the regime. The head of the IRGC was listed last December by the UN Security Council as

supporting Iran's nuclear and missile programs. The IRGC's control and influence in the Iranian economy is growing substantially. More and more IRGC-associated companies are being awarded important government contracts. An IRGC company, for example, has taken over management of the airport and runways in Tehran, while another company has won the contract to build the Tehran metro system.

Iran's present integration into the world financial community allows it to support and facilitate its dangerous activities. The regime disguises its hand in terrorism and weapons proliferation through an array of deceptive techniques specifically designed to avoid suspicion and evade detection from the law-abiding international community. For example, Tehran uses front companies and intermediaries to engage in ostensibly innocent commercial transactions that are actually related to its WMD programs. These front companies and intermediaries enable the regime to obtain dual-use technology and materials from countries that would typically prohibit such exports to Iran.

We have also seen Iranian banks request that other financial institutions take their names off of U.S. dollar transactions when processing them in the international financial system. This practice is even used by the Central Bank of Iran. This practice is specifically designed to evade the controls put in place by responsible financial institutions and has the effect of threatening to involve them in transactions they would never knowingly choose to settle. It can allow Iran's banks to remain undetected as they move money through the international financial system to pay for the Iranian regime's illicit and terrorist-related activities.

### TREASURY ACTION AGAINST IRAN

Because of the longstanding U.S. concerns about Iran's well-documented illicit behavior, the Treasury Department maintains broad sanctions against Iran. Although I want to focus today on our new, targeted sanctions -- or "measures" as I prefer to call them -- against individual bad actors, it is important to remember that the U.S. Government has maintained these general country sanctions for some time and that the new measures build upon our overall and long-standing Iran policy.

U.S. commercial and financial sanctions against Iran, which are administered by the Treasury's Office of Foreign Assets Control (OFAC), prohibit U.S. persons from engaging in a wide variety of trade and financial transactions with Iran or the Government of Iran. They prohibit most trade in goods and services between the United States and Iran, and any post-May 7, 1995 investments by U.S. persons in Iran. U.S. persons are also prohibited from facilitating transactions via third-country persons that they could not engage in themselves.

Beyond these general country sanctions, we are relying more and more on "targeted" measures directed at specific individuals, key members of the government, front companies, and financial institutions. These measures are aimed at specific actors engaged in specific conduct. Some require financial institutions to freeze funds and close the accounts of designated actors, denying them access to the traditional financial system. At times, the action includes bans on travel or arms transfers, which further confine and isolate those engaged in illicit activities. To maximize the effect, we try to apply these measures in concert with others. Whenever possible, we act with

a partner or a group of allied countries. We have done so, for example, in the context of U.N. Security Council Resolution 1737, which I will discuss shortly.

These kinds of measures have several advantages. Because they single out those responsible for supporting terrorism, proliferation, and other criminal activities, rather than apply to an entire country, they are more apt to be accepted by a wider number of international actors and governments. Targeted financial measures also warn people and businesses not to deal with the designated target. And those who might still be tempted to work with targeted high risk actors get the message loud and clear: if they do so, they may be next.

The United States is using various types of targeted measures to combat Iran's pursuit of nuclear weapons and development of ballistic missiles, as well as its support for terrorism.

First, while under our general Iran country sanctions program Iranian financial institutions are prohibited from directly accessing the U.S. financial system, they are permitted to do so indirectly through a third-country bank for payment to another third-country bank. In September 2006, we cut off one of the largest Iranian state-owned banks, Bank Saderat, from any access, including this indirect, or "u-turn," access to the U.S. financial system. This bank, which has approximately 3400 branch offices, is used by the Government of Iran to transfer money to terrorist organizations. Iran has used Saderat to transfer money to Hizballah. Iran and Hizballah also use it to transfer money to E.U.-designated terrorist groups, such as Hamas, the PFLP-GC, and the Palestinian Islamic Jihad. Since 2001, for example, a Hizballah-controlled organization received \$50 million directly from Iran through Saderat.

We have also acted against 19 entities and individuals supporting Iran's WMD and missile programs, including another Iranian bank, Bank Sepah, using Executive Order 13382. That Executive Order, signed by President Bush in June of 2005, 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 E.O. 13382 effectively cuts the target entity or individual off from access to the U.S. financial and commercial systems and puts the international community on notice about the threat they pose to global security as a result of their activities. Specifically, such a designation freezes any assets that the target may have under U.S. jurisdiction and prohibits U.S. persons from doing business with it.

While most states do not have a similar national-level designation authority as a tool to stem proliferation, they do now have binding obligations, which are similar to those under our Executive Order, under U.N. Security Council Resolution 1737. That resolution contains an annex listing entities and individuals responsible for Iran's nuclear and missile programs, and requires states to freeze their assets and the assets of entities owned or controlled by them.

Five of the U.S. designations against Iranian entities and individuals under E.O. 13382 have been similarly designated under UNSCR 1737. And, where our designations are not matched by designations at the United Nations, I can tell you that they still receive a great deal of international attention. I have traveled all over the world, sharing our list of Iran-related designations with foreign government counterparts and private sector representatives, and stressing the importance of ensuring that these proliferators are not able to access the

international financial system. Our list of targeted proliferators is incorporated into the compliance systems at major financial institutions worldwide, who have little appetite for the business of proliferation firms and who also need to be mindful of U.S. measures given their ties to the U.S. financial system.

The Treasury's designation of Iran's state-owned Bank Sepah under E.O. 13382 in January of this year is particularly significant because it makes it more difficult for the regime to hide behind its banks to support its proliferation activities. Like certain other Iranian banks and entities, Bank Sepah has engaged in a range of deceptive practices in an effort to avoid detection, including requesting that other financial institutions take its name off of transactions when processing them in the international financial system.

Bank Sepah provides direct and extensive financial services to Iranian entities responsible for developing missiles capable of carrying weapons of mass destruction. It has been a key provider of financial services to the Shahid Hemmat Industries Group (SHIG) and the Shahid Bakeri Industries Group (SBIG), two Iranian missile firms listed in the annex to UN Resolution 1737 for their direct role in advancing Iran's ballistic missile programs. Bank Sepah also provides financial services to SHIG's and SBIG's parent entity, Iran's Aerospace Industries Organization (AIO), which has been designated as a proliferator by the United States for its role in overseeing all of Iran's missile industries. AIO's Director is listed in the annex of Resolution 1737, thereby requiring states to freeze his assets as well as the assets of entities under his ownership or control.

Since at least 2000, Bank Sepah has provided a variety of critical financial services to Iran's missile industry, arranging financing and processing dozens of multi-million dollar transactions for AIO and its subordinates. The bank has also facilitated business between AIO and North Korea's chief ballistic missile-related exporter, KOMID. Also previously designated by the Treasury, KOMID is known to have provided Iran with missile technology. The financial relationship between Iran and North Korea, as reflected in the business handled by Bank Sepah, is indeed of great concern to the United States.

#### PRIVATE SECTOR RESPONSE

As I mentioned, aside from these "formal" actions, the Treasury has engaged in unprecedented, high-level outreach to the international private sector, meeting with more than 40 banks worldwide to discuss the threat Iran poses to the international financial system and to their institutions. Secretary Paulson kicked off this effort last fall in Singapore, in discussions during the annual IMF/World Bank meetings, where he met with the executives from major banks throughout Europe, the Middle East, and Asia. Secretary Paulson, Deputy Secretary Kimmitt, Assistant Secretary for Terrorist Financing and Financial Crimes Patrick O'Brien, and I have continued to engage with these institutions abroad, as well as in Washington and New York.

Through this outreach, we have shared information about Iran's deceptive financial behavior and raised awareness about the high financial and reputational risk associated with doing business with Iran. Our use of targeted measures has aided this effort by allowing us to highlight specific threats. We share 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 we want to isolate those actors and prevent them from abusing the financial system.

By partnering with the private sector, including by sharing information and concerns with financial institutions, we are increasingly seeing less of a tendency to work around sanctions. As I have traveled and met with bank officials abroad, I have learned that even those institutions that are not formally bound to follow U.S. law pay close attention to our targeted actions and often adjust their business activities accordingly for two main reasons. First, regardless of the underlying law in any particular country, most bankers truly want to avoid facilitating proliferation, terrorism, or crime. These are responsible corporate citizens. Second, avoiding government-identified risks is simply good business. Banks need to manage risk in order to preserve their corporate reputations. Keeping a few customers that we have identified as terrorists or proliferators is not worth the risk of facing public scrutiny or a regulatory action that may impact on their ability to do business with the United States or the responsible international financial community.

As evidence of Iran's deceptive practices has mounted, financial institutions and other companies worldwide have begun to reevaluate their business relationships with Tehran. Many leading financial institutions have either scaled back dramatically or even terminated their Iran-related business entirely. They have done so of their own accord, many concluding that they did not wish to be the banker for a regime that deliberately conceals the nature of its dangerous and illicit business. Many global financial institutions have indicated that they have limited their exposure to Iranian business. A number of them have cut off Iranian business in dollars, but have not yet done so in other currencies. It is unclear whether this is just a first step toward phasing out the business entirely. Regardless of the currency, the core risk with Iranian business – that you simply cannot be sure that the party with whom you are dealing is not connected to some form of illicit activity – remains the same. Scaling back dollar-business reduces, but does not eliminate, the risk.

As further evidence of the change in tide, a number of foreign banks are refusing to issue new letters of credit to Iranian businesses. And in early 2006, the OECD raised the risk rating of Iran, reflecting this shift in perceptions and sending a message to those institutions that have not yet reconsidered their stance.

Additionally, many other companies have scaled back on their investments or projects in Iran, concluding that the risks of expanding operations in the country are too great. Multinational corporations have held back from investing in Iran, including limiting investment in Iran's oil field development. These companies have done their risk analyses, and they have realized that the Iranian regime's behavior makes it impossible to know what lies ahead in terms of Iran's future and stability.

If Tehran chooses to continue on its current path, this is a trend that will continue. Iran's increasing isolation is the result of its own costly behavior. These are costs that the regime is not only imposing on itself, but also the Iranian people. Targeted financial measures, coupled with the private sector's reevaluation of its business with Iran, have sparked a debate inside Iran about the wisdom of the regime's policies. It is our hope that the Iranian regime will realize that the only way to rejoin the community of responsible nations is to change its behavior.

## CONCLUSION

Mr. Chairman, the Treasury Department – working closely with the State Department and the rest of the interagency – is playing an integral role in the Administration’s Iran strategy. Our use of targeted financial measures, along with outreach to the private sector about the risks of doing business with Iran, are indeed having an impact on the Iranian regime’s ability to misuse the financial system to carry out its dangerous activities. To be sure, the threat posed by Iran remains significant, but it is not insurmountable. We have made important progress on countering this threat, and we will continue working diligently to take all prudent steps to respond expediently to this challenge.

I look forward to working closely with you, other Members of the Committee, and your staff on this important issue. Thank you again for the opportunity to testify today.