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Keynote Address -- The Progression of Sanctions, A Historical Perspective

Richard Newcomb

KEYNOTE ADDRESS – THE PROGRESSION OF SANCTIONS, A HISTORICAL PERSPECTIVE

CHRISTOPHER SANDS: Michael, we truly wouldn't have been able to do [this program] without you. Thank you very much. Now, we go to our first keynote of the day, and it's a chance for me to introduce my former boss, Governor James Blanchard.

GOVERNOR JAMES BLANCHARD: Thank you, Chris Sands, for your leadership, Mark Green, for your directorship, and Dean Scharf. Thank you all. I happen to be a proud member of the Canada-U.S. Law Institute Executive Committee. I have the privilege for the first time, even though we've worked together for fifteen years, to introduce our keynote speaker, Richard Newcomb, known affectionately as Rick, and I want to get this right because he has been a leader in international law for several decades.

Rick led the international practice group at the global law firm of DLA Piper for 15 years. He's a world-renowned international lawyer, an expert in sanctions, of course. He led the Office of Foreign Assets Control at the Treasury Department. Rick led that for eighteen years. He oversaw thirty-nine different economic sanction programs that are intended to further our U.S. foreign policy interests in our security goals. I might add his work received acclaim and distinguished awards from three presidents: President Reagan, and my favorite president, Bill Clinton, who appointed me ambassador to Canada, so of course, he's my favorite. We have people joining this forum via Zoom from Montreal, Toronto, Calgary, all over Canada, Cleveland, and Detroit. We're pleased with this attendance.

I want to highlight the fact that Rick has been recognized as a distinguished executive by President Reagan, President Clinton, and President George H.W. Bush. He also received the highest award the Treasury Department can ever give. He is a dear friend. Rick is a proud graduate of Case Western Reserve University Law School, earlier Kenyon College, the alma mater of Paul Newman. I'm pleased to introduce a proud graduate of Case Western Reserve University Law School and a member of the Executive Committee of the Canada-U.S. Law Institute. Please welcome Rick Newcomb.

RICHARD NEWCOMB: Thank you, Jim, for that very kind introduction. It's most appreciated. It is indeed an honor and privilege to be here. This morning I've been asked to provide a brief background overview of the progression of primary and secondary sanctions over the past several decades.

In doing so, I'll provide the context and historical perspective on how we got to where we are now, highlighting the primary and secondary use of economic sanctions as one of the primary weapons in the arsenal of options available to the President of the United States in the conduct of his duties, in response to a threat from outside of the United States to the national security, foreign policy or the economy of the United States.

The history of the use of economic sanctions by the U.S. in the conduct of foreign affairs is rich, with an abundance of examples in the use of this tool. The

U.S. has led this effort over the years, and during our lifetime, has developed the tools and allocated the resources to build the administrative apparatus and support structure to make this an ever more effective option for the President when world peace is threatened following these key components:

- A strong and coordinated domestic enforcement;
- Strong compliance by major corporate and financial institutions;
- An administrative body or bodies capable of carrying out the Presidential mandate, principally through the issuance of regulations and guidance to define and strengthen the parameters of each sanctions program;
- Evermore effective use of intelligence and law enforcement assets and resources;
- A strong legal foundation with effective and flexible laws;
- Support and encouragement from the U.S. Congress with new legislation as needed, and sometimes when not needed;
- Wide deference by the courts to the Executive Branch on carrying out its foreign policy and national security objectives, strong Executive Branch political involvement; and
- Most important of all, a stable and dependable currency that the world relies upon as the currency of choice for the international trade of goods and services.

The U.S. has all of these, and that has enabled the U.S. to use its jurisdiction over U.S. persons, under primary sanctions, domestically, and economic strength to impose secondary sanctions extraterritorially.

To be clear about the distinctions: primary sanctions is the assertion of U.S. jurisdiction over U.S. persons wherever in the world they are located and over any person in the United States. I'll get to secondary sanctions in a moment. Talking about primary sanctions: the use relating to modern economic sanctions were first tested under the Trading with the Enemy Act, a 1917 statute, which was a predecessor statute to the authority [subsequently] used against Cuba, North Korea, Vietnam, Cambodia, China, and the Axis Powers during World War II.

Over the years, the courts established deference to the Executive and the carrying out U.S. foreign policy and national security with respect to the use of economic sanctions. They've evolved over this time and expanded under the International Emergency Economic Powers Act (IEEPA), enacted in 1977 for use during peacetime. The first test of this new statute, IEEPA, occurred during the Iran hostage crisis of 1979, when fifty-two U.S. nationals were taken hostage and the Iranian finance minister threatened to withdraw Iran's deposits from U.S. banks and attack the U.S. dollar in foreign exchange markets. The U.S. responded swiftly with a freeze of Iran's assets, which ultimately proved to be some $12 billion of funds and other property—a princely sum at that time.

On January 20, 1981, upon the inauguration of Ronald Reagan as President and the signing of the Algiers Accords, the hostages were freed, and a process was initiated to unfreeze assets and address U.S. and Iranian financial and commercial claims and counterclaims. Over the next several years, following the unanimous U.S. Supreme Court decision *Dames & Moore v. Regan*, U.S. private and corporate bank claims against Iran were settled. Many, especially U.S. bank claims, at or near one-hundred cents on the dollar. The Algiers Accords between the United States and Iran provided for the establishment of the Iran-U.S. Claims Tribunal to hear government-to-government claims between Iran and the U.S. It is the largest and most successful claims settlement program of its kind.

Flush on the success of the first Iran sanctions effort, there followed a series of other IEEPA-based programs. These included [against] Nicaragua, South Africa, Libya, Iran again, Panama, Sudan, Syria, Iraq, Kuwait, Myanmar, narcotics traffickers, terrorist organizations, and numerous other country and global law enforcement program initiatives. My focus will be on Iran, Russia, and the sanctions requirements imposed by the U.S. Congress.

In 1995, the President again imposed economic sanctions on Iran, this time for its support of terrorism and its terrorist activities. The 1995 Iranian sanctions initially were promulgated to prevent a U.S. oil company from completing its then-lawful contract with Iran to develop the rich South Pars oil field in Iran. When the U.S. oil company was ousted from Iran by executive order, other non-U.S. oil companies were poised to fill the vacuum and reap the windfall. In response, Congress, in 1996, decided that extraterritorial U.S. sanctions, or secondary sanctions, would help ensure that no other foreign company could do this, and passed the Iran and Libya Sanctions Act, referred to at the time as ILSA, and then only ISA when sanctions on Libya were removed. The law was perceived by foreign oil companies and their host governments as an overwhelming extraterritorial assertion of U.S. economic power. Significantly, however, ILSA had a presidential waiver provision, and enforcement was waived some forty or more times, every time a non-U.S. oil company engaged in such work in Iran, by succeeding administrations. Not until late in the Obama Administration, with the enactment of several new laws, did the Obama Administration come to apply "secondary sanctions" affecting non-U.S. banks and non-U.S. oil companies' dealings with Iran.

Secondary sanctions began as a menu of options available to the President under IEEPA or other related authority, including especially and most effectively, the use of the OFAC-specially designated national program. That is, the naming of specific non-U.S. persons or entities acting for or on behalf of the target country, person, or entity or the threat of so naming non-U.S. persons as SDN. The threat is a key issue. The practical effect of this threat is to make OFAC programs extraterritorial by forcing non-U.S. entities to cease transactions with such persons or run the risk of being cut off from all ties with the U.S., including especially from the U.S. financial system. Other lesser steps from the menu could be taken as well.

Again, I'll stress the threat of designation and the loss of access to the U.S. financial system [and] financial markets. Being blacklisted as an SDN is what creates the desired chilling effect. World trade in goods and services is conducted primarily in U.S. dollars, and international banks rely heavily on access to U.S. correspondent account relationships. No multilateral financial institution or corporation can run the risk of being cut off from the U.S. and the U.S. economy; they would go bankrupt if they were. Thus, we have secondary extraterritorial sanctions.

A new phase in sanctions development under IEEPA followed on the heels of the terrorist attacks of September 11, 2001. Then, President Bush declared comprehensive economic sanctions, along with other UN member states, against a new kind of target: Osama bin Laden, al Qaeda, and other terrorist groups acting worldwide in what would soon be described thereafter as the global War on Terror. The Treasury Department and the Office of Foreign Assets Control were called upon to administer them, working with other key elements of the U.S. government: law enforcement, intelligence, the diplomatic and military communities, and U.S. allies. The financial War on Terror sought to disrupt the flow of funds, business relationships, and transactions of any nature whatsoever with terrorist groups, their members, and support structure.

When members of the Congressionally mandated 9/11 Commission issued a follow up report in 2005 on U.S. response to the attacks of September 11 and its global War on Terror, it graded the five government elements: military, law enforcement, intelligence, diplomatic, and finance. Of these five elements, the financial War on Terror got the highest grade—an A rating—while the other four received scores ranging from "B" to a failing grade.

The Bush Administration got the message and became particularly aggressive in the use of economic sanctions as a tool of national security and foreign policy, especially in the wake of September 11th and the high marks the 9/11 Commission gave the financial war on terror. Efforts were redoubled by the Obama, Trump, and Biden administrations which have used sanctions as the primary tool in the conduct of U.S. foreign policy, reaching new levels and sanctions against Russia following the invasion of Ukraine.

Economic sanctions became a prime weapon for the Bush and Obama Administrations, especially in the War on Terror and in dissuading Iran from the pursuit of nuclear weapons, stopping Russia from further incursions into Ukraine, and other nations by severely restricting new debt or equity to a specific sector of the Russian economy: defense, metals, mining, oil, and gas. Especially for the purported annexation of Crimea, and then comprehensive sanctions with the war in Ukraine.

The Trump Administration continued this as well, in tightening primary and secondary sanctions against Russia, then Venezuela, North Korea, and in reimposing secondary sanctions against Iran and refusing to certify Iran's compliance with the Joint Comprehensive Plan of Action.

With regard to the many sanctions initiatives on Iran and Russia, the level and complexity of these programs, as they have evolved, is both comprehensive and targeted. Comprehensive in the sense that virtually all economic activity between U.S. persons and Iran has stopped and are heavily regulated since 1995. But especially now, in the case of Russia, targeted also with an interesting twist, and that is extraterritoriality. Secondary sanctions have evolved over this period of years and served as the model for Iran and now Russia as the sanctions architecture has evolved.

I'll go back and cite the statutes that were passed by Congress that gave the President this authority to move as he did. Starting in 2010, the U.S. government, both Congress and the Executive branch, sharpened the choice for non-U.S.

financial institutions. If they continue to conduct certain business with Iran, they risk losing access to the U.S. financial system and much more. Congress enacted new legal authorities to restrict correspondent banking or impose broader sanctions on non-U.S. banks that continued conduct with certain businesses with Iran.

To briefly summarize an explanation of how these multiple branches coordinated in their efforts against Iran and how this became the model for U.S. secondary sanctions, I'll start with the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010, known as CISADA. It empowered the U.S. Treasury Secretary to prohibit or impose conditions on opening or maintaining U.S. correspondent or payable-through accounts to foreign, non-U.S. financial institutions found to knowingly engage in sanctionable activities, including those entities that facilitate Iran's WMD acquisition or development, its support for international terrorism, or significant transactions with Iran's Islamic Revolutionary Guard Corps, or other large commercial enterprises.

This was followed the next year by the National Defense Appropriations Act, which essentially replicated this CISADA focus on transactions with designated banks but added the Central Bank of Iran as a new criterion for sanctions, as well as crude oil purchases. The following year, the Iran Threat Reduction Act amended the Iran Sanctions Act to add a new criterion for the imposition of secondary sanctions on persons doing business in Iran's energy or weapons sector. Then the following year, the Iran Freedom and Counter-Proliferation Act substantially expanded the already robust framework of U.S. sanctions against Iran, particularly U.S. extraterritorial sanctions on the energy, shipping, and shipbuilding sectors. This was the authority it needed to be acting upon. Acting pursuant to these newly established secondary sanctions laws, it was the U.S. that imposed sanctions that contributed significantly to the JCPOA, the Joint Comprehensive Plan of Action, the U.S. conclusion of the agreement itself, and the subsequent withdrawal that constitutes the next major chapter in the history of U.S. secondary sanctions.

In June of 2013, President Obama further tightened the economic embargo against Iran by targeting the activities of non-U.S. financial institutions and commercial businesses. This broke new ground by threatening to freeze the U.S. assets of non-U.S. persons who engage in transactions with certain Iranian government agencies and enterprises. The Executive Order that did this expanded the threat to the U.S. automotive sector, again, counterpart to the second most important business sector in Iran, in transactions that provided material assistance to certain persons blocked under laws and regulations. With this threat, the JCPOA was concluded between Iran, the United States, the United Kingdom, France, China, Russia, and Germany – so P7+1 – in July of 2015, and went into effect the following January. This agreement outlines specifics regarding how Iran must limit its nuclear power activity to make sure its programs do not result in the creation of nuclear weapons. The JCPOA lifted all secondary sanctions that had been in place against Iran but did not lift U.S. primary sanctions. However, in August of 2018, President Donald Trump issued an Executive Order and with it, the withdrawal of the U.S. from the JCPOA, reinstating sanctions against Iran, pursuant to the various legal authorities that were waived or lifted as part of the U.S. commitment under the JCPOA.

Since that time, the U.S. had been working with Iran to [conclude] a new nuclear agreement. However, recent events, notably [Iran's] sale of drones to Russia and the mass demonstrations highlighting the treatment of women by the so-called morality police, ended this dialogue some months ago. Now, with the ongoing war in Israel and Iran's expected support for it, that hope is now over.

Congress's expanding role has taken a more active stance in U.S. secondary sanctions, even those traditionally under the purview of the President in his conduct of foreign affairs. Iran serves as a good example here again. But there are other cases that I want to specifically point out where Congress has used legislative targeting against Hezbollah, Russia, North Korea, and others, inserting greater control. Congress has assumed this control by requiring that the President make determinations as to whether very specifically defined conduct has occurred. Upon making such determinations, Congress has then requiring the President to implement sanctions for which Congress has provided the parameters. There are three examples of this.

First, with regard to Hezbollah, the President is required to prescribe relevant regulations on the opening or maintaining of correspondent accounts or payable-through accounts by U.S. foreign financial institutions that the President determines to have engaged in any conduct with Hezbollah.

Second, perhaps most important, is the 2017 Countering America's Adversaries Through Sanctions Act (CAATSA), which requires the President to sanction targeted Iranian, Russian, and North Korean sectors and penalize non-U.S. persons for direct or indirect support of them. Under CAATSA sanctions dealing with Russia, it requires the President to impose secondary sanctions on foreign persons and financial institutions that engage in certain transactions with U.S.-sanctioned Russian parties or in sanctioned Russian activities, such as corruption, human rights abuses, sanctions evasion, certain crude oil projects, and Russian energy pipelines. It also includes parameters to make mandatory previously discretionary secondary sanctions involving two prior Russian U.S. sanctions laws involving Ukraine.

Third, the Global Magnitsky Human Rights Accountability Act is perhaps the greatest example of purely unlimited extraterritoriality. Its passage exemplifies that the extraterritorial reach of U.S. sanctions will continue to expand. To briefly summarize, the Global Magnitsky Act, signed into law in December of 2016, is an expansion of the Sergei Magnitsky Rule of Law Accountability Act of 2012. The original statute enabled the U.S. government to sanction individuals from the Russian Federation for torture, extrajudicial killings, and other human rights violations. The bill was named after Sergei Magnitsky, the lawyer who died in prison from police abuse and neglect after exposing fraud by members of the Russian government.

The Global Magnitsky Act expands the scope of potential sanctions from covering just Russian nationals to covering persons worldwide who engage in human rights abuses or corruption. Together, officials of the Treasury and State Department are empowered to prohibit entry into the United States and freeze assets of individuals located anywhere in the world considered responsible for corruption and human rights violations – it is a truly remarkable step. The President now has broad authority to blacklist any person of any nationality, wherever located, if there is reason to believe that they are involved in fraud or human rights violations. This is the broadest expansion, to date, of Presidential extraterritorial power. Never in history have U.S. sanctions had such an active presidential interest and played such a direct role in the application of economic sanctions, [as seen in cases] such as North Korea, Iran, Cuba, Venezuela, terrorist groups, and now Russia due to its invasion of Ukraine.

To briefly summarize the sanctions on Russia since Russia's invasion of Ukraine: the U.S. and its allies and partners around the world have taken numerous incremental steps to impose costs on Russia for the war. [These measures include]:

- Immobilizing $300 billion worth of assets in the Central Bank of Russia, limiting the central bank's ability to aid the war effort and mitigate the impact of sanctions;
- Imposing sanctions on Russia's largest financial institutions and restricted dealings with banks and major players, representing 80% of Russian banking sector assets;
- Issuing more than 4000 new amended sanctions listings, targeting major players, the Russian defense industrial complex, and numerous other defense-related firms, as well as non-Russian entities that have provided material support to Russian defense procurement efforts;
- Determining eight sectors of the Russian Federation economy to be sectors in which persons who operate or have operated [and] can be subject to sanctions, namely the financial services sector; the aerospace, electronics, and marine sectors; the accounting, trust and corporate formation services, and management consulting sectors; and the quantum computing sector of the Russian Federation economy. These sector determinations complement pre-February 2022 sanctions administered by OFAC with respect to persons operating in the technology sector and the defense and related materiel sector of the Russian Federation economy;
- Prohibiting new investment on the export of certain goods and services to persons located in Russia, including dollar-denominated banknotes, and accounting, management, and trust formation services.

The IEEPA basis for the Russia program, including the impact of an Executive Order issued by President Biden in April of 2021 (nine months before the invasion), has served as the basis for the many succeeding Executive Orders targeting Russia. The features of these Executive Orders provide wide discretion to the President to isolate Russia from the global financial economies and identify a broad range of sectors of the Russian economy as the predicate for primary and secondary sanctions. The reach of these new Russian sanctions relates to parties, financial and technological support for those primarily sanctioned, by providing a broad incursion into the power and chilling effect of secondary sanctions. The threat, fear, and deployment of extraterritorial and secondary sanctions have increased dramatically in recent years, as evidenced by the topics discussed this morning and by some of these factors.

First, going back to the passage of IEEPA in 1977, which specifically conferred broad power upon the President to declare a national emergency under IEEPA because of a threat, in whole or in part, from outside of the United States to the foreign policy, national security, or economy. The Act, in effect, confers on [the President] the authority to define the emergency and in the broadest terms declare what steps to take. The President is required to report to Congress and make the declaration in an annual report. But, keep in mind, the President sets the foreign policy of the United States and can decide what threatens it, as well as the national security and economy. Under the IEEPA, the President has virtually unfettered authority to conduct foreign affairs as he (or she) sees fit by the declaration of a national emergency.

However, upon looking at the legislative history, Congress never contemplated such a sweeping use of the power to deal with trade issues over the more traditional use of legal authorities for sanctions. The context in 1977 was on the heels of the Church Committee, which sought to repeal the Trading with the Enemy Act of 1917 due to its broad misuse by multiple administrations for a variety of other non-"Trading with the Enemy Act" purposes.

The second point pertains to the growing use of doctrines, such as causing a violation, which provides additional enforcement clouds based on IEEPA principles that the Department of Justice seeks to expand jurisdiction extraterritorially. This doctrine of "causing a violation" would occur when a foreign party, like a bank, misinforms a U.S. party as to what a transaction or a transfer involves. If it involves a misdescription or incorrect answers as to why the transaction occurred, there is jurisdiction to prosecute that foreign party foreign bank for causing the U.S. to violate a statute.

The powerful thrust and expanding use of secondary sanctions against non-U.S. entities, as illustrated by CAATSA, as well as the affiliates under OFAC "50% rule", and the final point is the politicization of sanctions.

The standard for designation on the OFAC blacklist is "reasonable cause to believe," and the administration decides what is reasonable based on all available sources of information. We are well aware neither intelligence nor law enforcement sensitive information, in and of itself, is evidence. Nevertheless, it is increasingly used as the basis for blacklisting non-U.S. persons for alleged acts, effectively denying review to the targeted person. Typically, there is no discovery because it is not a criminal charge. Moreover, intelligence information is not releasable, except in camera before a judge if it ever gets to that point. Thus, there is little, if any, opportunity to effectively challenge without commonly understood notions of due process.

Before I close, I want to leave several thoughts that I always share with audiences, especially commercial audiences, but I think would be relevant here, especially in the U.S.-Canada context.

First, for each sanctions program, know the rules because each one is different. No two sanctions are ever the same. All OFAC sanction programs are subject to strict liability and are very heavily permitted to impose criminal and civil penalties for violations. Keep in mind, that every sanctions program is promulgated by different people, at different times, for different specific foreign policy reasons. So necessarily, they're all going to be different. Thus, it's critically important for all U.S. banks and all U.S. corporations, or anyone doing business worldwide, to have a compliance program that is reviewed, continuously improved, and updated based on an ongoing risk assessment.

Know all the facts of any transaction that may touch on any sanctions program or sanctioned person. OFAC compliance is a very fact-intensive exercise. No two fact patterns are ever the same. I get together often with people that used to work for me in the OFAC compliance unit and we laugh. They're now with the major banks around the world. There's one thing we're able to agree on—they've never seen two fact patterns ever the same. They're always different.

Know your customer, its owners, directors, and managers. Know your customers' customers and their customers down the supply chain, direct to the delivery of goods.

If doing business internationally, check the OFAC SDN list for all transactions and understand the fifty percent rule. Anything owned 50% or more by a blocked person is itself blocked, whether it's listed or not on the OFAC SDN list. Surprisingly, there are some service providers that are able to do that and, within a matter of a minute or less, check out who all the parties are that are involved.

Enhance due diligence if and when necessary to assure yourself and partners, including banks. Check all sources and keep a record. Pay attention to red flags. Stop whenever you see one and investigate. Don't let yourself be willfully blind. If you find a violation, report it to OFAC, the U.S. State Department, or the Justice Department, depending on the facts.

Banks in the U.S. and around the world are de-risking. Even if authorized, banks increasingly will not process a transaction involving or touching a sanctioned country or do business with anyone that has unlawfully done business with a sanctioned person or country.

Understand there's a significant amount of lawful business between U.S. companies, with Iran and Russia, and other sanctioned countries, and know the difference. If in doubt about how to proceed, seek expert counsel.

Finally, as I said earlier, I want to make one additional point. There's a reason why the U.S. President has sanctions in his toolbox as an effective enforcement tool for the conduct of foreign affairs—the U.S. dollar. Since at least World War II, it has served as the world's reserve currency. International trade and goods predominantly is dominated in U.S. dollars – approximately 70 percent or more. Oil trades in dollars, it's dependable, especially as goods trade on the high seas, commodities trade—the U.S. dollar is the one currency they can depend on. Countries and banks around the world rely on it. Most international banks are *totally* dependent on U.S. correspondent banking relationships, and if they lose that because of a sanctions violation, which has happened, they're out of business. Period. This is a tremendously powerful tool for the U.S. when world peace is threatened. Should the reliability, dependability, or reputation become uncertain, through overuse of sanctions or default to meet debt obligations, the U.S. could lose this considerable leverage it has over the international banking system. Other currencies are available, but should a default occur, it's doubtful they could pick up the very important role the U.S. has had all these years.

I'll leave it at that. I look forward to the program today and will answer any questions you may have. It's exciting to have this session, and I thank you all.