Written Testimony of
Department of the Treasury Under Secretary David S. Cohen
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on Banking, Housing, and Urban Affairs

"Assessing the P5+1 Joint Plan of Action with Iran: Administration Perspectives"

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Introduction

Chairman Johnson, Ranking Member Crapo, and distinguished members of the Committee: Thank you for the opportunity to appear before you today to discuss the Department of the Treasury's ongoing efforts, along with our colleagues throughout the Administration, to isolate and pressure the Iranian economy; the temporary, limited and reversible relief offered Iran in the Joint Plan of Action (JPA); and the mounting sanctions pressure that Iran will face while the parties seek a comprehensive and long-term resolution to the international community's concerns over Iran's nuclear program. Our continued collaboration with Congress and this Committee in particular, is critical to our success in addressing this pressing national security issue.

The Impact of Sanctions

From the outset of the Obama Administration, we have pursued a dual-track strategy that pairs an offer to Iran to reclaim its place among the community of nations with increasingly powerful and sophisticated sanctions if it continues to refuse to satisfy its international obligations with respect to its nuclear program.

As this Committee is well aware, for several years Iran resisted and refused multiple opportunities to engage in a meaningful fashion. And so, as we made clear from the outset, the Administration, working alongside our international partners, has imposed on Iran the most comprehensive, powerful and effective set of sanctions in history. Today, Iran stands isolated from the international banking and financial system with slashed oil revenues, a withering energy production infrastructure, and a significantly diminished economy.

The enormous pressure presently applied on the Iranian economy did not come about overnight. We have worked hand-in-hand with Congress — including with this Committee — to construct a complex and comprehensive set of sanctions that focuses on those supporting Iran's nuclear and ballistic missile programs and, more broadly, Iran's key sources of economic strength. We maximized the impact and efficacy of our sanctions framework through robust engagement and outreach to foreign governments and the private sector. And we have aggressively enforced these sanctions by targeting illicit actors and their networks both inside and outside Iran.

While sanctions have proved to be a very potent tool, we have not imposed sanctions for sanctions' sake. One of the key purposes of sanctions always has been to induce a shift in the policy calculus of the Iranian government and to build the necessary leverage for serious negotiations about Iran's nuclear program.

Our dual-track strategy has begun to bear fruit. Sanctions pressure brought Iran to the negotiating table in Geneva and provided our negotiators with bargaining power to secure important limitations on Iran's nuclear program in the JPA. These limitations are the first meaningful limits Iran has accepted on its nuclear program in nearly a decade. But the deal is only a first step.

The limitations on Iran's nuclear program under the JPA create the time and space to test whether Iran is prepared to negotiate a comprehensive, solution that would give us assurance that Iran is not producing a nuclear weapon. Over the next six months, while we test this proposition, we will continue to apply intense pressure on Iran's economy by aggressively enforcing the vast majority of our sanctions that will remain in place. Unless Iran takes concrete and verifiable steps to prove that its nuclear program is exclusively peaceful, it will face increasing sanctions pressure and deeper isolation.

Limited, Temporary, and Reversible Relief

My colleague, Under Secretary Sherman, provides a detailed description in her testimony of the various commitments made by Iran in the JPA to halt, and in several important respects roll back, its nuclear program, while also allowing increased transparency and monitoring.

In short, Iran has committed to neutralize its entire stockpile of near-20 percent enriched uranium; cap its stockpile of 3.5 percent low-enriched uranium; halt all enrichment of uranium above five percent; limit its production and installation of centrifuges; and not make any further advances in its activities at the IR-40 Heavy Water Reactor near Arak. Tehran further committed to open its nuclear facilities to increased IAEA inspector access to give the world confidence that it is meeting its commitments under the JPA and is taking the required steps to halt its weapons program. And it committed to this in exchange for limited, temporary, and reversible relief.

Let me explain what I mean by "limited, temporary, and reversible relief."

The relief offered Iran is <u>limited</u> in several important respects. First, under the JPA, we will allow Iran access to a set amount of its own money – $4.2 billion in installments over the six-month course of the JPA – in a carefully controlled manner. Second, we will suspend some sanctions to allow Iran to engage in specified additional commercial activity – petrochemical exports, imports for its automobile industry, and gold trade – that altogether have at best marginal economic value to Iran. And third, the vast bulk of our sanctions, including the core oil, financial, and banking sanctions that have had such a dramatic impact on Iran's economy, remain in place and will continue to exert pressure on Iran's decision makers over the next six months.

The relief offered Iran in the JPA is also <u>temporary</u> in that it expires at the end of six months. At the end of six months, no additional funds will be made available to the Iranians, and the suspended sanctions will snap back into place. Because the JPA is renewable only "by mutual consent," at the six-month mark we could then consider whether, and to what extent, to provide additional relief to the Iranians in light of the circumstances. But if we decide not to provide additional relief, the relief described in the JPA expires at the end of six months.

And the relief in the JPA is <u>reversible</u>. If Iran fails to fulfill its commitments under the JPA, or refuses to enter into a comprehensive, long-term solution, we can stop the gradual release of funds, reimpose the suspended sanctions and impose new and enhanced types of sanctions.

The Relief Package

The relief package described in the JPA is composed of several discreet elements, as follows:

<u>Access to Restricted Funds</u>

The majority of the relief will come from granting Iran access, in installments over the six-month tenure of the JPA, to $4.2 billion of its own funds currently held in bank accounts outside of Iran – funds to which Iran has limited access and which right now can only be used for bilateral trade or humanitarian purchases. Let me underscore this point. These funds already belong to Iran, but under the international sanctions framework cannot be moved to third countries (except to facilitate humanitarian trade) nor repatriated to Iran. Not a single dollar of U.S. taxpayer money will be provided to Iran.

<u>Temporary Pause in Reduction of Iran's Crude Oil Sales</u>

We have agreed to hold Iran's exports of crude oil flat for a period of six months rather than requiring further significant reductions in the amount of Iranian oil purchased by oil-importing countries. To be clear, this will not allow Iran to increase its oil exports. To the contrary, Iran will be held to its currently depressed levels, down 60 percent from what it was selling in early 2012. This provision, moreover, will apply only to Iran's six current crude oil purchasers – Japan, Republic of Korea, China, Taiwan, India and Turkey. They will not be allowed to increase their purchases and no other country will be allowed to begin importing Iranian oil.

<u>Temporary Suspension of Petrochemical Sanctions</u>

U.S. sanctions on Iran's petrochemical exports will be temporarily suspended as part of this first step deal. We estimate that this will allow Iran to generate a maximum of $1 billion in new revenue over the next six months, but only if Iran is able to produce additional petrochemicals for export (some of its petrochemical plants have been retrofitted to boost gasoline production capacity for the domestic market) and only if Iran is able to find additional petrochemical customers – who typically prefer stable, long-term supply contracts – willing to sign contracts with Iranian exporters knowing that the sanctions are suspended under the JPA for only six months.

<u>Temporary Suspension of Sanctions on Iran's Auto Industry</u>

We will also temporarily suspend U.S. sanctions on exports by third countries to Iran's automobile industry. We estimate that this could provide Iran some $500 million in revenue, assuming Iran can resume prior levels of production and revitalize its car exports. Iran's automobile industry, however, is riddled with structural problems and was in steep decline even before our auto sanctions were put in place. Moreover, if Iran hopes to revive its auto sector, it would need to spend some of its limited foreign currency to pay for car kits from abroad.

Temporary Suspension of Gold Sanctions

Sanctions on Iran's ability to buy and sell gold will also be temporarily suspended. However, we expect that this provision will be of limited value to Iran because the only funds Iran can use to buy gold are its limited unrestricted hard-currency reserves. Because of the sanctions architecture that remains in place, Iran will be permitted to use neither its restrained foreign reserves nor its own currency, the rial, to buy gold. As a consequence, any gold Iran purchases would be offset by the hard currency it would spend to buy it, resulting in negligible economic benefits.

Limited Access to Funds for Tuition Purposes

Under strict guidelines, we will allow Iran to transfer $400 million of restricted Iranian funds to defray tuition costs for Iranian students studying outside of Iran, and will ensure that these funds are used for their intended purpose.

License Safety-Related Repairs And Inspection for Certain Airlines in Iran

We will license the supply and installation of spare parts for safety of flight, as well as safety-related inspections and repairs for certain Iranian aircraft, to occur in Iran. Previously, we had licensed these activities for Iranian aircraft only outside of Iran. Notably, Mahan Air, an Iranian airline that has been designated by Treasury for providing financial, material and technological support to Iran's Islamic Revolutionary Guard Corps-Qods Force and Lebanese Hizballah, will not be permitted to benefit from these repairs, nor would any other entity subject to sanctions under our counter-terrorism authorities.

Financial Channel to Facilitate Humanitarian Trade

Finally, we will assist in establishing a financial channel to facilitate humanitarian trade in food, agricultural commodities, medicines, medical devices for Iran's domestic needs, and to pay for the medical expenses of Iranian citizens incurred abroad. This will not provide Iran access to any new source of funds, because humanitarian trade with Iran is not targeted under existing sanctions authorities and because we intend that funds for medical expenses will come from Iran's limited stores of unrestricted hard currency. Humanitarian transactions have been explicitly exempted from sanctions by Congress and U.S. law places limits on the President's ability to regulate such trade.

The Relief Package in Context

The total value of the relief package – approximately $6 billion to $7 billion – will not materially improve the condition of the Iranian economy. Indeed, at the end of the six-month period, we expect that Iran will be even deeper in the hole economically than it is today due to the continuing and mounting impact of the sanctions we have in place and that we will continue to energetically enforce.

Indeed, the limited relief offered Iran in the JPA is dwarfed by the depths of Iran's economic distress. Our oil, financial and banking sanctions, in particular, have driven Iran into a deep recession. Since 2011, oil sanctions imposed by the EU and the U.S. have forced Iran's oil exports to decline from about 2.5 million barrels per day at the end of 2011 to about 1 million barrels per day today – costing Iran roughly $80 billion in lost sales. In that same period, Iran's currency, the rial, has lost around 60 percent of its value against the dollar. Approximately $100 billion of Iran's foreign exchange holdings are restricted or inaccessible due to our financial and banking sanctions. Over the last year, inflation in Iran has been about 40 percent. All told, last year Iran's economy contracted by more than five percent, and we expect Iran's economy to contract again this year. By contrast, according to the IMF, the economies of Iran's neighboring oil exporting competitors expanded last year by an average of over five percent and are expected to grow by an average of almost four percent this year.

These macroeconomic indicators reflect the impact of sanctions on, and the deep structural problems with, Iran's economy, none of which will be solved by the limited relief agreed to in Geneva. Indeed, over the six-month duration of the JPA, our oil sanctions alone will cost Iran an additional $30 billion (i.e., 4-5 billion per month) in lost revenue, which far surpasses the total sum of the relief package. Even taking into consideration the modest relief package, these staggering figures represent a bleak reality for Iran's economy, which we expect will continue to deteriorate over the next six months.

The International Sanctions Regime Remains Robust

We and our international partners will continue to impose increasing pressure on Iran's economy through the implementation and enforcement of sanctions, the overwhelming majority of which are not affected at all by the JPA. This includes the core architecture of our oil, financial and banking sanctions, which remain firmly in place.

Throughout the duration of this first-step deal, we will continue to enforce sanctions to ensure that Iran's oil sales are held down at their current, greatly depressed levels. Moreover, our financial sanctions remain fully in place, in particular the sanctions imposed by section 504 of the Iran Threat Reduction and Syria Human Rights Act of 2012, which became effective on February 6, 2013, and that "locks up" Iran's oil revenue in the few jurisdictions that still import oil from Iran.

As a result, with the exception of the $4.2 billion in funds that we will allow Iran to access in stages over the next six months, the revenue that Iran earns from its oil sales during the six-month duration of the JPA will remain subject to our financial sanctions. Those sanctions prevent Iran from using those funds for any purpose other than paying for goods from the oil importing country or humanitarian transactions. And any financial institution that facilitates a payment to Iran for oil imports beyond what is provided for in the JPA risks being cut off from the United States financial markets. In other words, over the next six months Iran cannot sell any more oil than its current levels, and any additional oil revenue it does earn (other than the limited funds to be made available under the JPA) will be locked-up and unavailable for transfer or repatriation.

In addition, the key banking sanctions imposed by the U.S. and the EU, which have resulted in the near-total isolation of Iran's financial sector, remain fully intact. That means that under Section 104 of the Comprehensive Iran Sanctions Accountability and Divestment Act of 2010, any foreign bank that engages in a significant transaction with Iran's designated banks risks losing its correspondent account access to the U.S. And it also means that all the banks designated by the EU will remain cut off from specialized financial messaging services, denying them access to critical networks connecting the rest of the international financial sector. Taken together, these sanctions – which remain fully in force – will ensure the continued isolation of Iran from the global banking system, and will continue to make it extraordinarily difficult to do business with Iran.

We also are focusing on enforcing additional elements of the U.S. sanctions program that deprive Iran of other sources of revenue. For example, sanctions will continue to constrict Iran's energy sector. Not a single prohibition or sanction on investment in Iran's energy sector will be suspended – for U.S. or international companies. All of the United States' sanctions on long-term investments in Iran's energy sector will remain in effect, as will the related sanctions on providing technical goods and services to the energy sector. This will ensure that Iran's oil and gas infrastructure remains severely impaired and increasingly obsolete.

Furthermore, all UN and EU designations, as well as our targeted sanctions on the more than 600 individuals and entities tied to the Government of Iran, its nuclear and ballistic missile programs and its energy, shipping, and shipbuilding sectors, remain in effect. Among other things, these sanctions mean that selling Iran cargo ships and tankers, providing insurance services or support for most Iranian shipping activities, providing flagging and classification services to Iranian ships, and helping Iran build port terminals or other facilities remain sanctionable activities.

In addition, sanctions remain in place against Tidewater Middle East Company, an IRGC-owned port operating company that manages the main container terminal at Bandar Abbas – which has been responsible for some 90 percent of Iranian container traffic and has operations at six other Iranian ports. These sanctions will continue to deter the export of products to Iran as well as the import of products from Iran.

This first-step deal also does not affect the longstanding U.S. trade embargo, meaning that Iran will continue to be shut out of the world's largest and most vibrant economy and precluded from engaging in business with U.S. companies and U.S. subsidiaries overseas.

Finally, it remains the case that Iran is the leading state sponsor of terrorism in the world today. Nothing in the JPA affects our continued efforts to contest and combat Iran's support of terrorism, its abhorrent human rights practices, or its destabilizing activities in Syria. All of our sanctions programs aimed at undermining this loathsome Iranian conduct remain active and energetic.

Vigorous Enforcement of Existing Sanctions

As President Obama said when he announced the JPA on November 23, "the broader architecture of sanctions will remain in place and we will continue to enforce them vigorously." This vigorous enforcement will be accomplished through the continued dedicated, resolute and creative work of professionals in our intelligence community, in the Treasury and State Departments, and across the Administration. We understand well the important role that sanctions pressure on the Iranian economy played in the lead-up to the JPA, and how important maintaining that pressure will be over the next six months as we explore the possibility of a long-term, comprehensive solution.

As I have just discussed, the vast majority of our sanctions remain in place, which we will continue to vigorously enforce, even as implement the JPA. We are determined to continue – in the days, weeks, and months ahead – to respond to Iran's evasion efforts, wherever they may occur, and to continue to aggressively enforce our sanctions.

For example, just yesterday, Treasury reached a $33 million settlement with the Royal Bank of Scotland plc for, among other things, apparent violations of U.S. sanctions on Iran and other sanctioned parties, including removing material references to U.S.-sanctioned locations or persons from payment messages sent to U.S. financial institutions. A few weeks ago we announced Treasury's largest settlement outside of the banking industry for violations of U.S. sanctions on Iran. As part of a combined $100 million settlement with several federal government partners, Weatherford International, Ltd. agreed to pay $91 million to settle its potential liability for extensive oilfield services provided in Iran from 2003 to 2007.

We believe our actions have put the international business community on notice: Iran is still off limits, including designated Iranian banks and businesses. Foreign banks and businesses still have to make a choice – they can do business with Iran, or they can do business with the U.S.— not both. I can assure this that we will continue to take action against those who evade, or attempt to evade, our manifold sanctions on Iran.

New designations and enforcement actions, moreover, are only one part of our strategy to ensure that the international business and banking community understands that now is not the time to expand activity in Iran. We have already begun a global campaign to ensure that foreign governments and the international private sector understand that the relief in the JPA is limited and targeted and that we and our partners are committed to ensuring that the pressure brought to bear on the Iranian economy remains robust. This campaign will continue in the weeks and months ahead, so that no one makes the mistake of believing that Iran is now open for business. It is not.

I have a clear message for every government, bank, business or broker that thinks now might be a good time to test our resolve: We are watching closely, and we are prepared to take action against anyone anywhere who violates, or attempts to violate, our sanctions.

Conclusion

As our negotiators seek a comprehensive solution to ensure that Iran's nuclear program is exclusively peaceful, Treasury and our partners across the Administration will continue to forcefully implement our sanctions programs to maintain crucial leverage at this pivotal moment. I look forward to continuing our work with Congress and this Committee as we pursue this vital objective.