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The US Declaration of War on Iran

A Chinese language version of this article is available at The Chinese Business Network

John McGlynn

March 20, 2008, destined to be another day of infamy. On this date the US officially declared war on Iran. But it's not going to be the kind of war many have been expecting.

No, there was no dramatic televised announcement by President George W. Bush from the White House oval office. In fact on this day, reports the Washington Post, Bush spent some time communicating directly with Iranians, telling them via Radio Farda (the US-financed broadcaster that transmits to Iran in Farsi, Iran's native language) that their government has "declared they want to have a nuclear weapon to destroy people." But not to worry, he told his listeners in Farsi-translated Bushspeak: Tehran would not get the bomb because the US would be "firm."

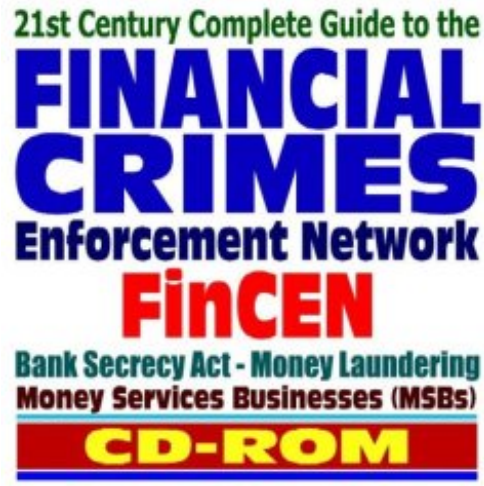
Over at the US Congress, no war resolution was passed, no debate transpired, no last-minute hearing on the Iran "threat" was held. The Pentagon did not put its forces on red alert and cancel all leave. The top story on the Pentagon's website (on March 20) was: "Bush Lauds Military's Performance in Terror War," a feel-good piece about the president's appearance on the US military's TV channel to praise "the performance and courage of U.S. troops engaged in the global war on terrorism." Bush discussed Iraq, Afghanistan and Africa but not Iran.

But make no mistake. As of Thursday, March 20 the US is at war with Iran.

So who made it official?

A unit within the US Treasury Department, the Financial Crimes Enforcement Network (FinCEN), which issued a March 20 advisory to the world's financial institutions under the title: "Guidance to Financial Institutions on the Continuing Money Laundering Threat Involving Illicit Iranian Activity."

FinCEN, though part of the chain of command, is better known to bankers and lawyers than to students of US foreign policy. Nevertheless, when the history of this newly declared war is someday written (assuming the war is allowed to proceed) FinCEN's role will be as important as that played by US Central Command (Centcom) in directing the wars in Afghanistan and Iraq.



In its March 20 advisory FinCEN reminds the global banking community that United Nations Security Council Resolution (UNSC) 1803 (passed on March 3, 2008) "calls on member states to exercise vigilance over the activities of financial institutions in their territories with all banks domiciled in Iran, and their branches and subsidiaries abroad."

UNSC 1803 specifically mentions two Iranian state-owned banks: Bank Melli and Bank Saderat. These two banks (plus their overseas branches and certain subsidiaries), along with a third state-owned bank, Bank Sepah, were also unilaterally sanctioned by the US in 2007 under anti-proliferation and anti-terrorism presidential executive orders 13382 and 13224.

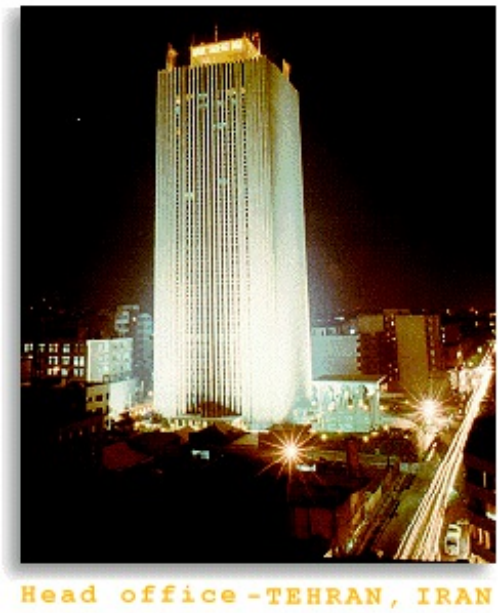
As of March 20, however, the US, speaking through FinCEN, is now telling all banks around the world "to take into account the risk arising from the deficiencies in Iran's AML/CFT [anti-money laundering and combating the financing of terrorism] regime, as well as all applicable U.S. and international sanctions programs, with regard to any possible transactions" with – and this is important – not just the above three banks but every remaining state-owned, private and special government bank in Iran. In other words, FinCEN charges, all of Iran's banks – including the central bank (also on FinCEN's list) – represent a risk to the international financial system, no exceptions. Confirmation is possible by comparing FinCEN's list of risky Iranian banks with the listing of Iranian banks provided by Iran's central bank.

The "deficiencies in Iran's AML/CFT" is important because it provides the rationale FinCEN will now use to deliver the ultimate death blow to Iran's ability to participate in the international banking system. The language is borrowed from Paris-based Financial Action Task Force (FATF), a group of 32 countries and two territories set up by the G-7 in 1989 to fight money laundering and terrorist financing. As the FinCEN advisory describes, in October 2007 the FATF stated "that Iran's lack of a comprehensive anti-money laundering and combating the financing of terrorism (AML/CFT) regime represents a significant vulnerability in the international financial system. In response to the FATF statement, Iran passed its first AML law in February 2008. The FATF, however, reiterated its concern about continuing deficiencies in Iran's AML/CFT system in a statement on February 28, 2008."

Actually, the February 28 FATF statement does not comment on Iran's new anti-money laundering law. The statement does say, however, that the FATF has been working with Iran since the October 2007 FATF statement was issued and "welcomes the commitment made by Iran to improve its AML/CFT regime." Moreover, the February 28 statement, for whatever reason, drops the "significant vulnerability" wording, opting instead to reaffirm that financial authorities around the world should "advise" their domestic banks to exercise "enhanced due diligence" concerning Iran's AML/CFT "deficiencies." In linking its March 20 advisory to the recent FATF statements, apparently FinCEN cannot wait for FATF or anyone else to evaluate the effectiveness of Iran's brand new anti-financial crime laws.

Anyway, the "deficiencies in Iran's AML/CFT" is probably the main wording FinCEN will use to justify application of one its most powerful sanctions tools, a USA Patriot Act Section 311 designation (see below).

Hammering away at Iran's state-owned banks is central to US efforts to raise an international hue and cry. Through its state-owned banks, FinCEN states, "the Government of Iran disguises its involvement in proliferation and terrorism activities through an array of deceptive practices specifically designed to evade detection." By managing to get inserted the names of two state-owned banks in the most recent UN Security Council resolution on Iran, the US can now portray the cream of Iran's financial establishment (Bank Melli and Bank Saderat are Iran's two largest banks) as directly integrated into alleged regime involvement in a secret nuclear weaponization program and acts of terrorism.



Bank Saderat

To inject further alarm, FinCEN accuses Iran's central bank of "facilitating transactions for sanctioned Iranian banks" based on evidence (which for various reasons appears true) gathered by Treasury and other US agencies that the central bank has facilitated erasure of the names of Iranian banks "from global transactions in order to make it more difficult for intermediary financial institutions to determine the true parties in the transaction." The central bank is also charged with continuing to "provide financial services to Iranian entities" (government agencies, business firms and individuals) named in two earlier UN Security Council resolutions, 1737 and 1747. In defense, Iran's central bank governor recently said: "The central bank assists Iranian private and state-owned banks to do their commitments regardless of the pressure on them" and charged the US with "financial terrorism."

So what does all this bureaucratic financial rigmarole mean?

What it really means is that the US, again through FinCEN, has declared two acts of war: one against Iran's banks and one against any financial institution anywhere in the world that tries to do business with an Iranian bank.

To understand how this works requires understanding what FinCEN does. This means going back in history to September 2005, when the US Treasury Department, based on the investigatory work of FinCEN, sanctioned a small bank in Macau, which in turn got North Korea really upset.

FinCEN's mission "is to safeguard the financial system from the abuses of financial crime, including terrorist financing, money laundering, and other illicit activity" (FinCEN website).

Under Section 311 of the USA Patriot Act the US Treasury Department, acting through FinCEN, has been provided with "a range of options that can be adapted to target specific money laundering and terrorist financing concerns." Specifically, Section 311 contains six "special measures" to significantly increase the powers of the Treasury (and other US government agencies) to block alleged terrorist financing activities. As explained by a Treasury official during April 2006 testimony before Congress, the most punitive measure requires:

> U.S. financial institutions to terminate correspondent relationships with the designated entity. Such a defensive measure effectively cuts that entity off from the U.S. financial system. It has a profound effect, not only in insulating the U.S. financial system from abuse, but also in notifying financial institutions and jurisdictions globally of an illicit finance risk.

On September 20, 2005 FinCEN issued a finding under Section 311 that Banco Delta Asia (BDA), a small bank in the Chinese territory of Macau, was a "primary money laundering concern." BDA was alleged to have knowingly allowed its North Korean clients to use the bank to engage in deceptive financial practices and a variety of financial crimes (such as money laundering of profits from drug trafficking and counterfeit US $100 "supernotes").

By publicizing its allegations, FinCEN let the world know that BDA was now at risk of having all "correspondent relationships" with US banks severed, a disaster for any bank wanting to remain networked to the largest financial market in the world. Frightened BDA

customers reacted by staging a run on the bank's assets.

In the interest of self-preservation, BDA was forced to act. After a quick conference with Macau financial authorities the bank decided to freeze North Korean funds on deposit.

It just so happened that the day before the FinCEN finding was made public the US and North Korea, working through the Six-Party talks process (also involving host China, Russia, South Korea and Japan), had formally agreed on a new diplomatic roadmap that promised to lead to a denuclearized and permanently peaceful Northeast Asia. But because of Treasury's BDA sanctions, North Korea was now labeled an international financial outlaw and the Six Party process stalled.

Other banks began severing their business ties with North Korea, leaving the country more isolated than ever from global commerce and finance. These other banks had no choice. Treasury repeatedly made clear that any bank that continued to do business with North Korea was another potential Patriot Act Section 311 target.

In anger, North Korea withdrew from the Six-Party process. It required 18 months of negotiations before a diplomatic and financial approach was devised that left BDA blacklisted but allowed North Korea to regain access to its frozen funds and rejoin Six Party negotiations.

Neither FinCEN nor anyone else at Treasury has ever publicly produced any evidence in support of the financial crime allegations against BDA and North Korea (articles by this author on BDA, North Korea and Treasury's lack of proof can be found at the Japan Focus website).

If Treasury was eventually forced to back off in the BDA case (apparently because the Bush administration changed its policy priorities), it had discovered that Patriot Act Section 311 could really shake things up.

The "real impact" of the BDA-North Korea sanctions, as Treasury undersecretary Stuart Levey told members of the American Bar Association in early March 2008, was that "many private financial institutions worldwide responded by terminating their business relationships not only with [BDA], but with North Korean clients altogether." Levey and his Treasury colleagues had come up with a way to go beyond governments to use the global banking sector to privatize banking sector sanctions against an entire country (this, by the way, is presidential candidate John McCain's proposed strategy for dealing with Iran as described in the Nov/Dec 2007 issue of the journal Foreign Affairs). This "key difference" in the "reaction by the private sector" was an exciting revelation. Through a little extraterritorial legal arm-twisting of the international banking community the US was able to put "enormous pressure on the [North Korean] regime – even the most reclusive government depends on access to the international financial system," said Levey. Washington now had "a great deal of leverage in its diplomacy over the nuclear issue with North Korea." Turning to the present, Levey informed the gathering of US lawyers that "we are currently in the midst of an effort to apply these same lessons to the very real threat posed by Iran." However, "Iran presents a more complex challenge than North Korea because of its greater integration into the international financial community."

Stuart Levey

Over the past two years Levey and other Treasury officials have been crisscrossing the globe to make it abundantly clear in meetings (described by Treasury as opportunities to "share information") with banking and government officials in the world's key financial centers that dealing with Iran is risky business. Levey frequently claims that major European and Asia banks, once they hear the US pitch, freely decided to cooperate with anti-Iran banking sanctions for reasons of "good corporate citizenship" and a "desire to protect their institutions' reputations."

But these meetings include quite a bit of browbeating. This can be deduced from some of Levey's public statements, such as his testimony to Congress. On March 21, 2007 Levey told the Senate Committee on Banking, Housing and Urban Affairs that unilateral US financial sanctions "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." Also, the possibility of becoming a Patriot Act Section 311 sanctions victim (which means exclusion from the US market) probably comes up at the meetings, as this part of his testimony indirectly suggests: "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."

Reportedly, Treasury Secretary Henry Paulson has also been involved in high-level meetings around the world concerning Iran, which presumably includes presentations on the arsenal of US financial sanctions. The message he imparts is unknown, but hints of the likely content can be found in public statements. Among Treasury officials Paulson has used the most dramatic language by making the argument that not only is Iran a danger to the international community but that this danger permeates virtually all of Iranian society. In a June 14, 2007 speech to the Council on Foreign Relations he first makes the point that Iran's Revolutionary Guard Corps (IRGC) is a "paramilitary" organization "directly involved in the planning and support of terrorist acts, as well as funding and training other terrorist groups." Then he offers the alarming revelation that the IRGC "is so deeply entrenched in Iran's economy and commercial enterprises, it is increasingly likely that if you are doing business with Iran, you are somehow doing business with the IRGC." With such language, Treasury lays the groundwork for applying financial sanctions against the entirety of Iran. All this makes clear that the growing coalition of bankers against Iran the US likes to trumpet may not be such a willing group.

Some indication of how unwilling can be found in the pages of Der Spiegel (English edition). In July 2007 the German news magazine reported that "anyone wishing to do business in the United States or hoping to attract US investors had best tread softly when it comes to Iran. Germany's Commerzbank stopped financing trade with Iran in US dollars in January, after the Americans piled on the pressure."

One German banker interviewed said: "German financial institutions feel the United States government has been engaging in 'downright blackmail'." The magazine goes on to report: "Anti-terror officials from the US Treasury are constantly showing up to demand they cut their traditionally good relations with Iran. The underlying threat from the men from Washington is that they wouldn't want to support terrorism, would they?"

Also, an April 2007 report from the UK's House of Lords Economic Affairs Committee states that the Confederation of British Industry indicated "strong concern" about Patriot Act provisions and other US extra-territorial sanctions. The Committee recognized the need for "vigorous action" in response to terrorist threats but also "endorse[d] the condemnation by the EU of the extra-territorial application of US sanctions legislation as a violation of international law."

Thus the US will need help from European government leaders to overcome resistance among major European financial institutions to US-led financial sanctions. Such help has already come from German Chancellor Angela Merkel. During her recent state visit to Israel, Merkel told the Knesset that Iran was global enemy number one. "What do we do when a majority says the greatest threat to the world comes from Israel and not from Iran?" she asked. "Do we bow our heads? Do we give up our efforts to combat the Iranian threat? However inconvenient and uncomfortable the alternative is, we do not do that." Iran is public enemy #1 in the world, and everyone – including the European banking establishment it would seem – has to accept that.

To summarize to this point: (1) the March 20 advisory represents a US declaration of war by sanctions on Iran and a sanctions threat to the international banking community, (2) the US has various unilateral financial sanctions measures at its command in the form of executive orders and Patriot Act Section 311 and (3) the BDA-North Korea sanctions were, at least in retrospect, a test run for Iran.

If the US succeeds, an international quarantine on Iran's banks would disrupt Iran's financial linkages with the world by blocking its ability to process cross-border payments for goods and services exported and imported. Without those linkages Iran is unlikely to be able to engage in global trade and commerce. As 30% of Iran's GDP in 2005 was imports of goods and services and 20% was non-oil exports (World Bank and other data), a large chunk of Iran's economy would shrivel up. The repercussions will be painful and extend well beyond lost business and profits. For example, treating curable illnesses will become difficult. According to an Iranian health ministry official, Iran produces 95% of its own medicines but most pharmaceutical-related raw materials are imported.

With a financial sanctions war declared, what happens next? There have been some hints.

On February 25 the Wall Street Journal reported that Treasury was considering sanctioning Iran's central bank (known as Bank Markazi). "The central bank is the keystone of Iran's financial system and its principal remaining lifeline to the international banking system," explains the Journal. "U.S. sanctions against it could have a severe impact on Iranian trade if other nations in Europe and Asia choose to go along with them." In anticipation of future events, the Journal notes: "U.S. officials have begun trying to lay the groundwork for a move against the central bank in public statements and meetings with key allies."

So look for the following to happen in the coming weeks: FinCEN will probably issue a Patriot Act Section 311 finding that Iran's central bank is a "primary laundering concern." The "deficiencies in Iran's AML/CFT" wording lifted from the FATF statement will be a key reason for that finding. The finding may be accompanied by a formal decision to cut off Iran's central bank from the US financial market, or such a decision could come later. Of course, an actual or threatened cut-off has no immediate financial implications for Iran since no Iranian-flagged bank is doing business in the US, except possibly to allow shipments from the US of humanitarian provisions of food and medicine, which, if they exist, probably terminate with the March 20 FinCEN announcement.

But a Section 311 designation of Iran's central bank would have a powerful coercive effect on the world's banks. For any bank in Europe, Asia or anywhere else that goes near the central bank once the 311 blacklist is on, it would be the kiss of death for that bank's participation in the international banking community, as it was (and remains today) for BDA. Not only would that bank be barred from the US financial market, it would also be shunned by European and Japanese financial markets, as government and private banking officials in those markets are likely to cooperate with Washington's intensifying sanctions campaign.

What about China, now one of the world's major financial centers (two Chinese banks ranked among the top 25 in The Banker's 2007 survey of world banks) and a major trading partner for Iran?

China and Japan "were the top two recipients of exports from Iran, together accounting for more than one-quarter of Iran's exports in 2006," according to an analysis of International Monetary Fund (IMF) trading statistics contained in a December 2007 US Government Accountability Office (GAO) report on Washington's anti-Iran sanctions regime. On the import side, the GAO found that in 2006 "Germany and China were Iran's largest providers of imports, accounting for 23 percent of Iran's imports." Airtight global banking sanctions imposed on Iran would presumably make the financial administration of this trade next to impossible.

Will China bend to US sanctions wishes? Early signs suggest the answer is yes.

In December 2007 ArabianBusiness.com reported that Chinese banks were starting to decline to open letters of credit for Iranian traders. Asadollah Asgaroladi, head of the Iran-China chamber of commerce, was quoted as saying that China's banks did not explain the refusal but "if this trend continues it will harm the two countries' economic cooperation and trade exchange." In February, ArabianBusiness.com found that China's cutbacks in its banking business with Iran was affecting a joint automobile production arrangement.

Such disruptions in the Chinese-Iranian banking relationship are minor. Meanwhile, Beijing keeps insisting that peaceful diplomacy with Iran is the best policy and that the only sanctions needed are those mandated under the three UN Security Council resolutions already on the books. Thus, to make China cooperate with Washington's unilateral banking sanctions, the US and the EU, reports the Financial Times, are apparently using a tag-team strategy.

On February 12 the FT told readers that "the US believes that tighter EU sanctions will put pressure on other nations that do more business with Iran - China for example - to curb their activities." Therefore, explained an anonymous diplomat apparently from the US: "We will be pushing the EU to go further than the Security Council," a move intended, the diplomat said, to "gold plate" Security Council requirements.

To explain this move the FT provided an example of "gold plating" from 2007, when the EU implemented UN Security Council resolutions 1737 and 1747 on Iran:

> "In similar language to the current text on Banks Saderat and Melli, the UN had called for "vigilance and restraint" concerning the movements of individuals linked to Iran's nuclear and missile programmes and members of its Revolutionary Guard. But in implementing the resolutions, the EU subjected all the named individuals to a travel ban - a much tougher measure."

Reading between the lines, the intention behind "gold plating" Security Council resolutions is to put pressure on China to bow to a more aggressive US-EU sanctions program. In the case of the most recent Security Council resolution on Iran, 1803, which put sanctions on two Iranian banks, FinCEN rolled two "gold plating" actions into one. It combined the Security Council's naming of the two banks with the October and February FATF statements to justify its March 20 warning to the world that Iran's entire banking system is a danger. Whether the EU will follow FinCEN's action, and how China will respond to any of this, remains to be seen.

In short, the US has in effect declared war on Iran. No bombs need fall as long as the US strategy relies solely on financial sanctions. But if the US Section 311 designates Iran's central bank as a financial criminal, the impact will be the financial equivalent to the first bombs falling on Baghdad at the start of the US-UK invasion of Iraq in March 2003.

In a 1996 publication written for the National Defense University, Harlan Ullman and James Wade introduced a military doctrine for "affecting the adversary's will to resist through imposing a regime of Shock and Awe to achieve strategic aims and military objectives."

Former US defense secretary Donald Rumsfeld made Shock and Awe famous by invoking it as the US strategy in the attack on Iraq in March 2003 (though weeks later Ullman was claiming Rumsfeld was misapplying the doctrine).

But Shock and Awe's authors (apparently with something like Vietnam or the 1993-1994 Somalia fiasco in mind) also envisioned that "[i]n certain circumstances, the costs of having to resort to lethal force may be too politically expensive in terms of local support as well as support in the U.S. and internationally." Consequently, they wrote:

> "Economic sanctions are likely to continue to be a preferable political alternative or a necessary political prelude to an offensive military step . . .ã€€In a world in which nonlethal sanctions are a political imperative, we will continue to need the ability to shut down all commerce into and out of any country from shipping, air, rail, and roads. We ought to be able to do this in a much more thorough, decisive, and shocking way than we have in the past . . . Weapons that shock and awe, stun and paralyze, but do not kill in significant numbers may be the only ones that are politically acceptable in the future."

It was only a matter of finding a sanctions strategy systematic enough to make this more obscure portion of the Shock and Awe doctrine operational. What Ullman and Wade could not have imagined was that Washington's global planners would use extraterritorial legal powers and its financial clout to coerce the global banking industry into accepting US foreign policy diktat. North Korea was a test-run for the new strategy of Shock and Awe financial sanctions. As Washington Post columnist David Ignatius put it in February 2007, "[t]he new sanctions are toxic because they effectively limit a country's access to the global ATM. In that sense, they impose -- at last -- a real price on countries such as North Korea and Iran."

What then will the impact be of this US-Iran banking standoff? For the US, almost no impact at all. Treasury bureaucrats will spend some time and a little taxpayer money making phone calls, checking computer screens and paper trails to monitor global banking compliance with sanctions. The cost of financially ostracizing Iran will be a bargain for US taxpayers compared with the eventual $3 trillion cost of the Iraq and Afghanistan wars estimated by Nobel prize-winning economist Joseph Stiglitz and Harvard financial expert Linda Bilmes.

Iran, however, will become another Gaza or Iraq under the economic sanctions of the 1990s, with devastating impact on economy and society. That Iran's complete financial and economic destruction is the goal of US policy was spelled out by the State Department the day before the FinCEN announcement.

During a daily press meeting with reporters on March 19, the State Department's spokesperson was asked about a deal recently signed between Switzerland and Iran to supply Iranian natural gas to Europe. After condemning the deal, the spokesperson explained that the US is opposed to any "investing in Iran, not only in its petroleum or natural gas area but in any sector of its economy" and questioned rhetorically the wisdom of doing business with Iranian "financial institutions that are under UN sanctions or could become under sanctions if it's found that they are assisting or aiding or abetting Iran's nuclear program in any way." A clearer expression of US desires is hardly possible.

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