

# ASSESSING U.S. SANCTIONS ON RUSSIA: NEXT STEPS

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## HEARING BEFORE THE COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE ONE HUNDRED FIFTEENTH CONGRESS FIRST SESSION ON

EXAMINING THE EXISTING RUSSIAN SANCTIONS ARCHITECTURE IN  
TERMS OF ITS EFFECTIVENESS AND ECONOMIC IMPACT AND ASSESS-  
ING WHAT CORRECTIVE ACTION, IF ANY, THE UNITED STATES  
SHOULD TAKE IN LIGHT OF RECENT DEVELOPMENTS INVOLVING  
RUSSIA'S ACTIONS IN UKRAINE, SYRIA, AND WITH CYBER ATTACKS  
TARGETED IN THE UNITED STATES

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MARCH 15, 2017

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## ASSESSING U.S. SANCTIONS ON RUSSIA: NEXT STEPS

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WEDNESDAY, MARCH 15, 2017

U.S. SENATE,  
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,  
*Washington, DC.*

The Committee met at 10:23 a.m., in room SD-538, Dirksen Senate Office Building, Hon. Mike Crapo, Chairman of the Committee, presiding.

### OPENING STATEMENT OF CHAIRMAN MIKE CRAPO

Chairman CRAPO. This hearing will come to order.

Today we will examine the existing Russian sanctions architecture in terms of its effectiveness and economic impact and assess what corrective action, if any, the United States should take in light of recent developments.

Three years ago this week, Russia solidified its actions in Crimea by illegally annexing the Ukrainian territory and moving the fight to its eastern border regions.

In response, the United States, the European Union, and several other allied countries imposed several rounds of targeted economic sanctions against Russia. And 2 years ago, the Obama administration imposed a separate set of sanctions against Russia in response to its malicious cyber-enabled information warfare activities.

Today the Committee will hear testimony on the effect and utility of these U.S.-imposed sanctions and the potential for next steps.

The existing U.S. sanctions against Russia pertaining to the Ukraine were designed to change Putin's behavior.

Authority for the sanctions is found in a series of four Executive orders issued in 2014, as well as in the Ukraine Freedom Support Act, which was signed into law in December of that same year.

These authorities prescribe asset freezes and transaction prohibitions with specific Russian individuals and entities with ties to the Kremlin, including a bank, businesses tied to Putin, and a state-owned defense company.

Sanctions also include restrictions on financial transactions, such as 1- to 3-month restrictions on debt maturities of Russian firms operating in the financial services, energy, and defense sectors.

The United States also restricts its individuals and entities from exporting oil-related goods, services, and technology in support of deep water, Arctic offshore, or shale projects in the maritime areas claimed by Russia.

Pursuant to these measures, the United States Department of Treasury has identified and designated more than 520 individuals

and entities for their sanctionable activities. Those persons designated are subject to the blocking or freezing of assets under U.S. jurisdiction, prohibitions on transactions with U.S. persons, and visa denials.

During the last 3 years, Russia was stung by the twin shocks of international sanctions and low oil prices. This was compounded by Russia's own ill-conceived retaliatory measures.

As a result, Russia is now challenged by a contraction of economic growth, capital flight, depreciation of the ruble, a higher rate of inflation, budgetary pressures, drawing on its international reserves, and more widespread poverty generally.

Yet Russia remains a hostile, recalcitrant power, deploying its military, cyber-enabled information espionage activities, and economic tactics to harm the United States and drive a wedge between it and its allies.

With all this in mind, I trust the witnesses today will help the Committee understand the impact of the existing sanctions generally, and discuss where the real pressure points are in Russia's economy, the costs of inaction, and any associated unintended consequences that could arise if sanctions were imposed either unilaterally or too rapidly.

The extent to which the sanctions on Russia alone contributed to its economic downturn is an important question in terms of preserving the existing sanctions or expanding the breadth of existing sanctions.

One thing is clear: Any reduction to the level of sanctions in the absence of a corresponding shift in Russian behavior will be interpreted as a change in U.S. policy on Russia's involvement in Ukraine, and that would run counter to the norms of international law and give Russia license to engage in further adventurism.

Russia must be held accountable for its actions, and if sanctions are to be a part of that strategy, they must be targeted and staged appropriately according to a set of realistic conditions.

With that, I conclude my opening statement and turn to Senator Brown.

#### **STATEMENT OF SENATOR SHERROD BROWN**

Senator BROWN. Thank you, Mr. Chairman. Sorry for being late.

Thanks for calling this hearing. Thanks for your willingness to explore on a bipartisan basis how the current U.S. and multilateral sanctions regime is working and possible next steps to strengthen it while preserving unity with our allies. Congress has worked together to craft the current U.S. sanctions regime and to hold Russia accountable for a long line of misdeeds from its violations of international law and of the sovereignty and territorial integrity of Ukraine to its role in the brutal repression of the war in Syria and its cyber attacks on the United States, including U.S. elections.

More recently, Russia has engaged in efforts to influence our elections and systematically sowed disinformation here at home. We should focus now on what the Committee might do to strengthen our response to Russia for the actions I mentioned and for its continuing efforts to destabilize states in Europe, including the Balkans and beyond.

Russia's interference in our election, confirmed unanimously by the U.S. intelligence community in a declassified report, as we know, in early January, poses a problem that goes far beyond foreign policy and strikes at the core of our democracy. As the joint report makes clear, there is no disagreement within the U.S. intelligence community about what happened here. None. Zero. They wrote:

Russian efforts to influence the 2016 U.S. Presidential election represent the most recent expression of Moscow's longstanding desire to undermine the U.S.-led liberal democratic order . . . these activities demonstrated a significant escalation in directness, level of activity, and scope of effort compared to previous operations.

We assess Russian President Vladimir Putin ordered an influence campaign in 2016 aimed at the U.S. Presidential election. Russia's goals were to undermine public faith in the U.S. democratic process, denigrate [Democratic candidate] Secretary Clinton, and harm her electability and potential presidency. We further assess Putin and the Russian Government developed a clear preference for President-elect Trump. We have high confidence in these judgments.

Those were words from the U.S. intelligence community.

The report went on to note that similar efforts would likely be undertaken by Russia against U.S. allies and others. "We assess Moscow will apply lessons learned from its Putin-ordered campaign aimed at the U.S. Presidential election to future influence efforts worldwide, including against U.S. allies and their election processes."

While we have begun to impose sanctions for Russia's cyber attacks, we have not yet responded to the interference with our electoral process. The Ukrainian community, rather large in Ohio, and around the world, knows firsthand the dangers of unchecked Russian aggression. We should strengthen, not weaken, Russian sanctions, and the President must work with Congress on a Russia policy that is clear-eyed about our adversaries and their behavior.

In Syria, the U.N. and others have charged Syrian military units and allied Russian forces with war crimes, including attacks on hospitals and an aid convoy, and indiscriminate bombing of civilian populations in eastern Aleppo.

The recent escalation of violence by Russian-based separatists in eastern Ukraine and the lack of a consistent policy to deter further Russian aggression is also dangerous.

Since Putin's illegal annexation of Crimea in 2014, 3 years ago this week exactly, there have been at least 10,000 dead, 20,000 wounded, 2 million internally displaced, according to the U.N. The situation remains unstable with some 300,000 cease-fire violations in 2016, according to the Organization for Security and Cooperation in Europe.

It seems clear from the surge of violence since the U.S. elections that Russia is testing our resolve to support the Ukrainian Government and people. We must leave no doubt that Russia must comply with the Minsk agreement. Until it does, Russia deserves no sanctions relief for the conflict it created and continues to fuel.

I hope the President ends any ambiguity in our policy in both his words and the vigorous enforcement and strengthening of current sanctions. All of us in both parties are very concerned about what the President has done or not done so far. So far, he has sent

mixed signals. On the one hand, he raises questions about moral equivalence between the United States and Russia and flirts publicly with relaxing Russian sanctions. On the other hand, he has said he intends for now to maintain U.S. sanctions, and U.N. Ambassador Haley has condemned Russian aggression in Ukraine.

Today we are joined by three sanctions experts who will help us assess where we are and what effects the current sanctions regime is having on the economy and the behavior of Russia. We will also discuss how stricter sanctions enforcement, closing administrative loopholes, strengthening statutory requirements where appropriate, and other measures can send a clear, unambiguous signal of our resolve.

I welcome the witnesses and thank the three of you for joining us.

Chairman CRAPO. Thank you very much, Senator Brown.

I would like to remind all of our Senators today to try to stay very close to the 5-minute time limit. We have a hard stop at about 5 minutes to 12, and I think we will have a lot of interest in this hearing, and so I encourage us all to pay close attention to the time restrictions.

And to our witnesses, I ask you to please pay attention to the 5 minutes as well. I know that you are not going to be done with everything you have to say in 5 minutes, but you are going to have a lot of opportunity with questions to get into it all.

Today we are joined by three excellent witnesses. First we will receive testimony from Ms. Elizabeth Rosenberg, who is the Senior Fellow and Director of the Energy, Economics, and Security Program at the Center for a New American Security.

Next we will hear from Mr. Eric Lorber, who is a Senior Advisor at the Center on Sanctions and Illicit Finance at the Foundation for Defense of Democracies.

And, finally, Dr. Rodney Ludema, Associate Professor of Economics at Georgetown University, will give us his assessment of the economic impact of the current sanctions regime.

Ms. Rosenberg, you may proceed.

**STATEMENT OF ELIZABETH ROSENBERG, SENIOR FELLOW  
AND DIRECTOR, ENERGY, ECONOMICS AND SECURITY PRO-  
GRAM, CENTER FOR A NEW AMERICAN SECURITY**

Ms. ROSENBERG. Thank you. Chairman Crapo, Ranking Member Brown, and distinguished Members of this Committee, thank you for the opportunity to testify today on Russia sanctions.

U.S. and European sanctions imposed on Russian entities and individuals since 2014 have been remarkably innovative and forceful. Responding to Russia's aggression in Ukraine, they powerfully demonstrate transatlantic unity, and they have delivered economic leverage. Their impact was augmented, as was noted, by an oil price collapse and Russia's resulting loss of hard currency.

Additional recent U.S. sanctions have exposed Russia's human rights record, its destabilizing involvement in Syria, and its insidious cyber intrusions into U.S. institutions and political processes.

The recent record of Russian economic performance demonstrates a period of distress. From the beginning of 2014 to December 2016, Russian external debt shrank from \$729 billion to \$519 billion, and



officials drew down the Reserve Fund from \$87 billion to \$16 billion. Russian officials slashed state spending in education, health care, and defense, and allowed the ruble to plunge in value. Capital fled Russia, roughly \$210 billion in 2014 and 2015 combined, and GDP contracted from 0.7 percent in 2014 to negative 3.7 percent in 2015. It recovered last year but remained negative.

Russian officials, including President Putin, have acknowledged that sanctions hurt Russia. They were a meaningful contributor to Russia's agreement to the Minsk accords, and Russia, arguably, refrained from more expansionist territorial aims because of sanctions pressure.

However, the force of sanctions has diminished over time as investors have adapted to lower oil prices, the Russian economy stabilized and U.S. and EU leaders have not kept up sanctions pressure. In 2016, Russian capital flight was one-tenth of the 2014 record. Russian economic growth is expected to rebound to just over 1 percent in 2017. Russia expanded its already massive energy output by 4.4 percent between January 2014 and January 2017, taking advantage of higher prices to draw in critical new revenue streams.

A primary reason for declining sanctions effects is a lack of their maintenance by the United States and the European Union. In particular, European leaders have struggled over the last 2 years to hold the line on sanctions, doubting their utility and advisability in some instances.

Now, political signals from the new U.S. administration as well as from nationalist political leaders in Europe that a warmer relationship with Russia may be forthcoming indicate to the private sector that sanctions are weakening further. Russia has actively taken advantage of this crumbling resolve on sanctions. Through military posturing, media and cyber manipulation, and economic interventions, President Putin has been transparently engaged in a reproach of Western interests and Western unity.

U.S. leaders are now contemplating policy toward Russia, including sanctions measures. The White House has not yet outlined a definitive strategy with the Kremlin or European allies. Congress is in the position to enhance pressure on Russia in response to increasing aggression in eastern Ukraine and Russia's cyber interference in the United States.

Legislators can lead on the direction for an updated sanctions response and set the tone for diplomacy toward European allies and Russian counterparts. To maintain effective sanctions, U.S. and European leaders must closely coordinate. This will be difficult, but the alternatives—stasis or conflicting sanctions policy, delivers economic and political benefits to President Putin and undermines U.S. interests. It is far preferable to maintain Western economic leverage with Russia and negotiate from a position of strength. In this context, U.S. leaders, with Congress at the fore, must proactively update sanctions and forge new transatlantic coordination on this critical policy challenge.

Thank you for the opportunity to speak with you this morning, and I look forward to your questions.

Chairman CRAPO. Thank you very much.

Next we will hear from Mr. Lorber.

**STATEMENT OF ERIC B. LORBER, SENIOR ADVISOR, CENTER  
ON SANCTIONS AND ILLICIT FINANCE, FOUNDATION FOR  
DEFENSE OF DEMOCRACIES**

Mr. LORBER. Chairman Crapo, Ranking Member Brown, and distinguished Members of the Senate Committee on Banking, Housing, and Urban Affairs, I am honored to appear before you today to discuss U.S. sanctions on Russia.

I would like to focus my testimony on the effectiveness of the current U.S. sanctions targeting Russia, as well as what the United States can do to responsibly ramp up economic pressure to convince Moscow to cease destabilizing activities in eastern Ukraine, stop committing human rights abuses, and reduce malicious cyber activities targeting the United States and its allies.

To date, U.S. sanctions on Russia have a mixed record of success. Many macroeconomic indicators and recent studies suggest that the sanctions have had an impact on overall Russian economic health. Likewise, Russian Government officials repeatedly push for sanctions relief, both in public statements and by trying to undermine EU sanctions, suggesting that Russia is feeling the pinch.

Nevertheless, the United States has not achieved many of the core objectives it sought when deploying these tools, and Russia continues to engage in threatening activity across a range of areas.

In eastern Ukraine, Russian-backed forces continue to violate the cease-fire, routinely attacking Ukrainian villages and military personnel. Moscow also continues to target opposition leaders, often with lethal means.

In the cyber realm, Russia has continued its efforts to influence and undermine U.S. allies, in recent months focusing these efforts on upcoming elections in Western Europe.

Beyond the activities for which the United States has imposed sanctions, in Syria, Russia continues to support President Bashar al-Assad with direct military intervention, including during the Syrian Government's brutal assault on Aleppo.

This Committee should make no mistake; Russian activity in these areas poses a serious threat to U.S. interests, and the United States should be prepared to use all elements of its national power—including its economic power—to blunt Moscow's ability to undermine U.S. interests at home and abroad.

Additional, responsibly crafted U.S. sanctions can be a powerful tool to impact Russia's decisionmaking. Specific types of sanctions that, if properly calibrated, could be particularly effective in increasing the pressure on Russia include:

The codification of certain executive orders, as well as additional statutory designations under these EOs;

Establishment of a FinCEN-led task force to identify and seize assets of targeted Russian persons, including those with close to ties to Russian President Vladimir Putin;

Certain restrictions related to the purchase or facilitation of Russian sovereign debt;

And certain primary and secondary sanctions on elements of Russia's oil and gas industry.

However, any new sanctions on Russia must take into account four important considerations.

First, while additional sanctions are appropriate, Congress should be wary of imposing sanctions that are too powerful. If the United States attempts to impose broad, Iran-like sanctions on Russia that target large swaths of the Russian economy, this could limit critical European willingness to participate in our sanctions campaign.

Similarly, such sanctions could do serious damage to the Russian economy in ways that actually threaten our interests. While we want to pressure Russia to cease its activities, destroying the Russian financial system or cratering its economy would have worldwide impact, threatening markets across the globe.

Second, Congress should think through how it can unwind sanctions pressure in the case that Moscow—even partially—changes its behavior. As we have learned over the past few years, unwinding sanctions can often be a difficult and fraught process. Any such new sanctions legislation could include built-in “off ramps”—namely, elements of the sanctions regime, such as specific designations or directives—that could be undone in a situation of partial Russian compliance with its various obligations, such as those under the Minsk agreements. Such partial sanctions relief could be traded for Russian fulfillment of these obligations, and this approach, while not achieving all of our objectives certainly, could help the United States limit challenges to U.S. interests.

Third, any such sanctions must be nested in a larger strategy of pressuring Moscow, including aggressive diplomacy and responding in kind to malign Russian activities such as offensive cyber operations. Sanctions are a means to an end, and Congress and the Administration must be clear as to what that end is and how they intend to achieve it. Ramping up economic pressure on Moscow without clear objectives, the employment of other coercive tools, and buy-in from the Administration is unlikely to be effective in getting Moscow to fully change its behavior.

Fourth, the United States must be prepared to address Russian retaliation for these sanctions, including in the form of counter-sanctions, increased cyber attacks, and even kinetic action in ways that threaten U.S. interests.

Congress has a key role to play in ramping up pressure on Moscow, and the various sanctions proposals put forth in recent weeks are excellent steps in this direction. I look forward to discussing these proposals during the question-and-answer session.

Thank you.

Chairman CRAPO. Thank you very much.

Dr. Ludema.

**STATEMENT OF RODNEY D. LUDEMA, Ph.D., ASSOCIATE PROFESSOR, SCHOOL OF FOREIGN SERVICE AND DEPARTMENT OF ECONOMICS, GEORGETOWN UNIVERSITY**

Mr. LUDEMA. Chairman Crapo, Ranking Member Brown, and distinguished Members of the Committee, thank you for the opportunity to testify at today’s hearing assessing U.S. sanctions on Russia. My name is Rodney Ludema, and I am a Professor of Economics at Georgetown University.

Earlier this year, my co-author Daniel Ahn and I published a report titled, “Measuring Smartness: Understanding the Economic

Impact of Targeted Sanctions,” and I would like to take this opportunity to share some of the conclusions of that study with you.

As you know, Russian intervention in Ukraine in early 2014 prompted the United States and the European Union to impose series of targeted sanctions aimed at specific individuals, companies, and transactions believed to be involved in the illegal annexation of Crimea and the ongoing crisis in eastern Ukraine. Sanctions of this type are often referred to as “smart,” and their defining feature is that they seek to impact their intended targets with minimal collateral damage.

Our study seeks to understand just how “smart” these sanctions have been in practice, and what we find is that the sanctions have indeed inflicted significant damage on the intended targets, with relatively little short-run impact on the overall Russian economy or on neighboring economies such as the European Union.

Just to put sanctions a little bit in context, decades of experience with economic sanctions indicate that sanctions are most effective at altering the behavior of the targeted government when they are multilateral, focused, sustainable, and clearly contingent on an achievable goal.

Smart sanctions are meant to achieve these ends. They are focused because they target the government and its domestic constituencies responsible for the offending policy rather than the general population, which may have little political influence.

They are sustainable because by minimizing collateral damage, they lower the cost to the countries imposing them, and this is especially important when we are talking about a target country that is large and internationally integrated, such as Russia.

So how do we go about assessing the smartness of Russian sanctions? First, we look at the sanctioned companies themselves. All told, we were able to find 584 companies that are either listed by the United States or the European Union in one or more of their sanctions lists or are associated with individuals on those lists. In addition, there are another 2,000 or so subsidiaries of these companies.

Our method is to compare the performance of sanctioned companies to nonsanctioned peer companies before and after the sanctions were imposed. Our main finding is that sanctioned companies are indeed harmed by sanctions relative to their nonsanctioned peers. On average, a sanctioned company loses an estimated one-third of its operating revenue, over half of its asset value, and about one-third of its employees after being sanctioned compared to nonsanctioned companies. These estimates suggest that the targeted sanctions do indeed have a powerful impact on the targets themselves.

The second part of our study estimates the collateral damage. In particular, we consider the impact that the sanctions have had on Russian GDP and on Russia’s imports from the European Union. The challenge in doing this is the fact that the conflict coincided with a series of powerful macroeconomic shocks, most notably an enormous decline in the price of oil, which is Russia’s main export.

We find that the vast majority of the decline in Russia’s GDP and the vast majority of its import demand from the European Union is caused by the decline in the price of oil and other

long-term trend factors, with very little left to be explained by sanctions or other short-term factors. Thus, we conclude that either sanctions have had only a small negative effect on Russia's GDP, as they were designed to do, or other positive factors coincident with sanctions largely canceled out their effect.

Finally, we find that sanctions have had only a small effect on the economies of most European countries. Adding together the impacts of sanctions imposed on Russia along with Russia's retaliatory countersanctions on agricultural products, we find that EU exports declined only slightly, causing less than two-tenths of 1 percent reduction in the GDP of the median EU country.

Those are the results of our study, and I am happy to entertain questions about that in the Q&A session. Thank you.

Chairman CRAPO. Thank you very much, Dr. Ludema.

Let me go first to you, Ms. Rosenberg. Moscow remains undeterred in its Ukraine ambitions despite at least 2 years of sanctions, which were even compounded by an oil shock. What are the limits of employing sanctions against a large economy like Russia's? And what sanctions tend to be the most effective to deter Russian aggression?

Ms. ROSENBERG. Thank you for the question. As you note, Russia is a massive economy, and even in the period from 2014 to now, when we have seen the Russian economy shrink somewhat, it still represents one of the largest economies globally. Furthermore, it has a tremendous volume of external assets that are traded actively, including by U.S. financial entities and individuals. So the cautionary note on sanctions is to be careful about collateral damage for the United States. Going after Russia, particularly in the financial services realm, in ways that could affect U.S. institutions may be damaging to U.S. economic interests. Also, if the United States oversteps and goes too far on sanctions, in addition to the consequences my colleague laid out, it could invite retaliation.

I would offer the same cautionary note about aiming too aggressively at its energy sector given the effect that that could have for consumers globally, including in the United States.

Chairman CRAPO. Thank you very much.

Mr. Lorber, some proposals put forth for increasing sanctions against Russia include various sanctions on Russian sovereign debt. Could you please explain what placing sanctions on entities transacting in issuances of Russian sovereign debt would have on the Russian economy and on global financial markets?

Mr. LORBER. Absolutely, Senator. The macroeconomic impact of going after prohibiting purchase or facilitation of Russian sovereign debt is fairly uncertain. However, what the impact likely would do is it would put additional pressure on those SSI designated entities from 2014 that have effectively been to an extent propped up by the Russian Government. So it would continue to target entities that we have gone after previously.

But the unknown about what the overall impact of sanctioning Russian sovereign debt would be is part of the reason that in my testimony I suggest ways that you can, in effect, ratchet up that pressure in a graduated manner so that you can, in effect, see what that impact is; and if the economic impact on those entities is not

what we want it to be, you can sort of come back and have a second bite at the apple.

Chairman CRAPO. Thank you very much.

Dr. Ludema, your study finds that while targeted firms are impacted by sanctions, Russia's GDP is largely unaffected, noting that the most plausible candidate factor for this would be the Russian policy response.

Explain what you mean by the "Russian policy response," and how do you think the Russians responded to the sanctions within this context?

Mr. LUDEMA. Thank you for the question. I would say that there are actually two reasons why the sanctions have had very little effect on the Russian GDP. One is that they were designed to not have an immediate effect. The biggest companies that are under sanctions are sanctioned under the SSI regime which simply restricts their borrowing of long-term debt and certain technologies. That is designed to kick in later as these companies start to roll over their debt. They are not likely to have a short-term effect, and we find that they generally do not.

But, yes, you are right; there are things that the Russian Government can do and has done to also counter the effects. For example, the biggest thing that they did was allow the ruble to depreciate quite dramatically in 2014.

Another thing that they can do is bail out certain firms, so they have a list of firms that they refer to as "strategic," that are strategic by virtue of their economic or national security importance, and these firms qualify for state largesse in the form of state loan guarantees, capital participation, extra government contracts, tax breaks, and so on.

I would point out, however, that all of these policy responses are costly to the Russian Government, so even if you see a company that is not obviously affected by Russia sanctions, if it is being bailed out, that cost is being imposed on the Russian Government in a different way. We have a saying in economics, which is that "There is no free lunch." And there is no free lunch for the Russian Government when it comes to dealing with sanctions.

Chairman CRAPO. Thank you very much.

Senator Brown.

Senator BROWN. Thank you, Mr. Chairman.

Ms. Rosenberg, if I could start with you, you described four principles you think policymakers should observe: maintaining broad support of allies; using sanctions as a tool, while including other diplomatic, political, economic, and military measures; tying sanctions relief tightly to specific policy goals; and, fourth, crafting a policy that is tough and constructive and also flexible enough to be workable.

What are the greatest obstacles to maintaining these principles on Russia policymaking in this environment?

Ms. ROSENBERG. Thank you for the question. One of those principles that is most vulnerable is finding unification and multilateralism on Russia sanctions. The reason why I say that is because of the conflicting political suggestions that we have seen coming out of the current U.S. administration, as has been mentioned by you. They suggest that there is an interest in pulling

back or reversing sanctions measures. Also signaling from within Europe, including from a couple of the leaders on European sanctions, France and in Germany, not to mention the Brexit vote, which suggests movement toward strong nationalism and away from the project of EU unification and transatlantic unity that has underpinned these sanctions on Russia.

The difficulty in holding together that coalition is the greatest challenge to advancing further strong, cogent, meaningful, and strategic sanctions policy.

Senator BROWN. You are suggesting, as I think you mentioned in the response to Chairman Crapo's question, that there is a danger—you may not have used the word “danger,” but you said if we are too aggressive, especially on energy, when you think of how bound so many countries, especially those that were long-time Soviet—a long time part of the Soviet Union, how bound they are, especially on energy. Talk about that effect with our allies and how other proposed measures imposing secondary sanctions on those who facilitate Russia Soviet debt transactions, how that plays out and what concerns you have and which countries are most affected that way.

Ms. ROSENBERG. On energy in particular, the challenge here about being too aggressive, I would like to condition that and say there are two challenges: one is being too aggressive too fast. It would be appropriate to move incrementally toward a more aggressive posture. The second one is that sanctions should always aim at what is realistically achievable. This is particularly important on energy where aiming too aggressively is infeasible ultimately. It would be impossible for the United States to implement aggressive sanctions on the Russian energy supply. European leaders would not join the United States on something that aggressive. For them, it would constitute a decision to cutoff some of their most significant energy supply sources. Literally, the lights go out, the heat goes off. That is a very difficult thing for many countries, particularly in Russia's near abroad, its periphery, that rely so heavily on Russian refined products and natural gas in particular. The energy market is so large and so many nodes and relatively unregulated globally that it would be near to impossible to achieve broad implementation; and even if it were, what it could do—even if there was to be broad implementation of strong sanctions that go after Russia's energy supply, it would have the effect of increasing prices, which some may welcome in the current oil price environment. But, of course, that benefits producers, including Russia, and disadvantages consumers, such as those in the Baltic States and all of us as consumers.

Senator BROWN. Thank you.

Real quickly, Mr. Lorber, talk about what conditions you think Russia should have to meet besides abiding by Minsk and stopping cyber attacks before any future relaxation of sanctions.

Mr. LORBER. Thank you, Senator. I actually think that the Minsk II agreement does provide for 13 very specific obligations that Russia should meet and, frankly, is not meeting at the current time. And so it gives us, in a sense, a road map for sanctions relief. If Russia meets these objectives, then we should be willing to provide them at least partial relief as—

Senator BROWN. They are meeting none of them now of the 13?

Mr. LORBER. That is my understanding, so the major ones, for example, allowing Ukraine to have control over the Ukraine-Russia border; the removal of heavy weaponry; the allowance of OSCE monitors into the country; the return of Crimea to Ukrainian control. My understanding is that they have not met—they have certainly not met those, but they have not met many of the others of the 13.

Senator BROWN. Thank you.

Chairman CRAPO. Thank you.

Senator ROUNDS.

Senator ROUNDS. Thank you, Mr. Chairman.

Mr. Lorber, I am just curious. We have talked a little bit about the issuance of sovereign debt and the challenges that we may place on the Russian economy and so forth if we were to restrict, either in a primary or primary and secondary basis, the purchase of Russian sovereign debt. How would that impact the individuals who are the decisionmakers or the impacters within Russia today? Would we be able to actually impact those individuals who are the decisionmakers?

Mr. LORBER. Thank you, Senator. I think so, yes. The rationale behind the sovereign debt restriction is basically that when Russian entities were designated as SSIs, they were unable to secure new debt or in some cases new equity. And so the Russian Government injected capital assets into them to basically keep them going, in effect. And then Russia turned around and wanted to offer sovereign debt issuances so that it could then continue injecting more funds into those SSIs and SSI entities.

To the extent that you can hurt those of the largest companies in Russia, the CEOs and major leaders of whom many are within Vladimir Putin's close inner circle, I do think that will have an impact on their decisionmaking.

Senator ROUNDS. How practical is the imposition of both primary and secondary attempts, anyway, at limiting the purchase of that debt? Would we have any support in the European Union?

Mr. LORBER. So I think that is actually a fantastic question because I think that in terms of the imposition of primary sanctions that would prohibit U.S. persons, or any transaction with a U.S. nexus, from going forward, from doing transactions in that debt. That would not directly impact foreign financial institutions in the European Union, for example, but there would still be a significant market impact. So many of the sort of top-line European banks, financial institutions, would be unwilling to transact in that debt for fear that they might accidentally run afoul of U.S. sanctions. So I do think that there would be a practical effect of it, yes.

Senator ROUNDS. Thank you.

Ms. ROSENBERG. Senator, may I speak to this issue?

Senator ROUNDS. Yes.

Ms. ROSENBERG. Thank you. I wanted to point out something that all policymakers contemplating this kind of a sanction should bear in mind going forward, which is, of course, that aiming at Russian sovereign debt is a major escalation. It may be appropriate as circumstances merit, but particularly because you are going after the ability of the sovereign to raise money, there will be a



major public perception in Russia and elsewhere that this will constrain the ability of Russia to provide social services. This has worked to President Putin's favor in bolstering his domestic popularity and support, and so this has to be carefully calibrated in order not to have the reverse effect, which is to say empowering President Putin at the expense of the pressure it is supposed to create.

Senator ROUNDS. I think your point is well made, and the reason why I asked the question is specifically that. Does the emphasis actually fall on the decisionmakers, or does it fall on the general Russian economy itself?

Let me just continue on, and I do have a question for Dr. Ludema. A significant portion of your testimony focused on smart sanctions and minimizing collateral damage, specifically as we just discussed with regard to the imposition of any sanctions on the purchase of sovereign debt.

As you know, the United States has implemented a ban on the investment and now prohibits essentially all trade with Crimea, which is, in essence, an embargo on Crimea.

To what extent does the U.S. trade and investment embargo on Crimea cause collateral damage on the average citizen of that Ukrainian population? And what role does this policy play in the grander strategy, of course, in Russia and Russian-supported groups to cease their malicious and destabilizing activity in the region? And does the value of this coercion outweigh the collateral damage to the majority of Crimea's Ukrainian citizens now under Russian rule? A three-part question.

Mr. LUDEMA. Thank you for the question. I think that if by collateral damage you mean damage to the general population in Crimea, I would say that there is collateral damage, certainly. Crimea is a relatively small entity so it does not have substantial impact on the European Union or the United States. And so in that sense, I think sanctions of that type would, nevertheless, remain sustainable.

I think the idea behind the sanctions on Crimea is that it will make it difficult for the Russian Government to solidify its control in the area, and I think that is the purpose of it. Whether it succeeds is something that is beyond that.

Senator ROUNDS. Thank you.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you.

Senator Reed.

Senator REED. Thank you very much, Mr. Chairman, and I want to thank the panel for their presence here today and their testimony.

Senator Rounds brought up the European Union, and I have just three general questions I would like to pose to everyone, beginning with Ms. Rosenberg. What is their role today? Second, can that role be enhanced to benefit the doing—and I presume they are—to undermine the European Union as they are trying to undermine so many institutions? So if you could generally respond to those questions. Ms. Rosenberg?

Ms. ROSENBERG. Thank you for the question. The role of the European Union as counterpart to the United States in imposition of

these sanctions is significant, primarily because it has great economic integration with Russia—trade, investment, *et cetera*, for banks, companies, and the like. So the EU's holding the line on these sanctions constitutes a bigger economic sacrifice for them in many respects, particularly for those countries heavily linked to Russia through trade on Russia's periphery.

The sanctions can be enhanced by the European Union, and, in fact, they are well placed to do so. There are a number of what have been referred to as loopholes in the European sanctions on Russia by comparison to the United States sanctions, involving the grandfathering of certain business and the availability of certain Russian firms to raise funds in European capital markets. That could be closed off. That would be at a great sacrifice to the European economy, one which many in Europe believe is worth it.

And what is Russia doing to undermine the European Union? What we witnessed in the United States in terms of Russia's malicious cyber intrusion into our electoral process in 2016 is occurring in Europe. It is active. It is well documented, including support for political parties and disinformation campaigns.

Senator REED. Just let me qualify. The European Union is an institution itself with an elected President, *et cetera*. Are they targeting the European Union as an institution as well as the countries?

Ms. ROSENBERG. I think it would be fair to characterize the effort by Russia primarily aimed at individual countries because giving rise to nationalist political currents in these individual countries undermines the project of European unification, which is Russia's aim, and undermines transatlantic unity.

Senator REED. Mr. Lorber and Mr. Ludema, any other comments that you think would supplement Ms. Rosenberg's comments?

Mr. LORBER. A couple. Thank you, Senator.

On the first point, what is the EU role, I agree with Ms. Rosenberg and would also like to say that the EU program is actually very, very similar to the U.S. program. They have an SSI type of program. They have a list of designations. There are a number of designations which are different, so they do not have a number of people on their list that we have on ours, and vice versa. And so that is one particular area where we could align better and have them ramp up pressure.

Also building off of her comments in ways that we can enhance the EU sanctions or have the European Union enhance their own sanctions, one area in particular is related to entities that are owned by Russian companies that are operating in the European Union. In general, these entities are not subject to the EU SSI sanctions, and that is a European decision to limit the damage to their economy. That could be a particular area where we focus on to have them go after.

And then on your last point, the question about what is Russia trying to do to undermine EU unity, in effect, in addition to the cyber activity Russia has engaged in and the empowerment of far right parties, Russia has actively engaged in trying to pull one or two EU countries out of the sanctions sort of cooperative regime, because EU voting rules require unanimity and the sanctions must be renewed every 6 months. They were actually renewed a couple

days ago. And to the extent that the Russians can basically buy off one or two EU countries, such as Hungary, that can actually undermine the entire sanctions campaign from the EU side.

Senator REED. Doctor, your comments?

Mr. LUDEMA. Yes. I think that EU participation in this has been extremely important. The European Union is much more integrated with the Russian economy than we are. They have potentially more influence, but, of course, they are also more sensitive when it comes to collateral damage.

On the question of what is Russia doing, they are constantly—constantly—filling the airwaves in Europe with negative news stories about the impact of sanctions on European companies, claiming way beyond the evidence that these things are having a devastating effect on European economies. And part of the reason that we wrote our paper was to demonstrate that, by and large, that is not true.

Senator REED. Thank you very much.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator.

Senator SASSE.

Senator SASSE. Thank you, Chairman. Thank you to all of you for being here.

How rich is Vladimir Putin?

Ms. ROSENBERG. We should assume very rich, although the amount of his assets has been a longstanding question. There is no full disclosure.

Mr. LORBER. Again, there is no full disclosure, so it is unknown. My understanding based on public source reporting is that it is in the billions, if not tens of billions of dollars.

Mr. LUDEMA. Yeah, I do not have a number on that either, but certainly his ability to tap into vast sums of money through his cronies and his network is—well, it is enormous.

Senator SASSE. Can you remind us of his sort of resume, his work history? How did he get rich?

Mr. LUDEMA. Corruption.

Mr. LORBER. I am not a Vladimir Putin expert, but, obviously, he was in the KGB as a colonel for a long time, and then—

Senator SASSE. They make tens of billions of dollars, right?

Mr. LORBER. They make tens of billions of dollars primarily through corruption and proceeds from state enterprises, is my understanding.

Senator SASSE. So could you bound the illicit economy for us in Russia? What are its key industries? And how did it happen? Give us sort of a sweep—you know, Nebraskans, when they think about the demise of the Soviet Union, we remember sort of Warsaw Pact versus NATO. And in 1989 the wall falls. In 1991 the Soviet Union dissolves. Nineteen ninety-one (1991) to 1994 or 1995, we have this vision that there is going to be this sort of rise of democratic capitalism in Russia. That does not happen. So from 1995 until maybe 2 years ago, give us a 20-year sweep of the Russian economy and sort of the role that illicit industries and cronies play. How does this develop?

[Pause.]

Senator SASSE. Not all at once, please.

Mr. LUDEMA. I will take a stab. I do not know if I would call them “illicit industries,” but certainly crony capitalism has been on the rise ever since Putin took power. One of the reasons, despite high oil prices, prior to the sanctions regime, despite high oil prices, the Russian economy was underperforming was precisely because of crony capitalism, that is, almost all of the big industries are controlled by Putin cronies. They used them as their personal piggy banks. They failed to invest adequately, and it has significantly sapped the dynamism of the Russian economy, such that even if oil prices were to recover and sanctions were to be removed, I do not think you would see a miraculous rebound of the Russian economy.

Mr. LORBER. Thank you Senator. Important, I think, to add to this point as well is that as Putin’s cronies were enriched and took over state-owned enterprises, Putin also privatized—or, sorry, made public certain Russian Government entities, oil-producing, and put his individual sort of inner circle in charge of them to see the proceeds. And then of particular note, I think, to this Committee, Russian oligarchs set up a large set of shell companies, of mechanisms for transferring illicit funds, and, frankly, got a lot of those funds out of Russia. And so we know now that through Cyprus and other jurisdictions with lax anti-money-laundering laws and regulations, Putin and his oligarchs have actually managed to get all these funds into Western economies, into real estate, both in the United States and in London and other parts of Western Europe.

Ms. ROSENBERG. I think my colleagues have offered a number of strong comments, and so I will not add more.

Senator SASSE. Great. Well, we would love to follow up with you. My team will reach back out, because I think one of the core questions we face is the efficacy of the current sanctions regime, the possibility of a new sanctions regime and its cooperation with EU and other members, but also to what degree is it going to be efficacious if we do not have a lot of clarity about other places where money is housed that is not actually on the books in ways that can be transparent. Please, take a final word. We have a couple seconds left.

Mr. LORBER. Thank you. The Counteracting Russian Hostilities Act of 2017 has a provision in it related, as I mentioned in my testimony, to a FinCEN-led task force or some type of task force to assess, identify, and eventually seize illicit funds that are in the United States. We know they are here; we just do not actually know where they are. And so I think that is one good proposal you could walk forward with.

Senator SASSE. We would love to figure out ways to assist you in the work of being more transparent about those assets. Thanks.

Chairman CRAPO. Thank you.

Senator MENENDEZ.

Senator MENENDEZ. Thank you, Mr. Chairman, for holding what I think is an incredibly important hearing, and I appreciate the testimony of the expertise we have here. I look forward to Administration witnesses so that we can actually move forward on developing policy at some point, but certainly this is incredibly helpful.

As the original author of many of the networks of sanctions that we have on foreign adversaries and belligerent actors, I certainly believe that economic sanctions remain one of the most effective tools we have in our peaceful diplomacy arsenal, which is rather limited. When you speak about nonmilitary engagement, it is the use of aid or trade to induce a country to act a certain way. International opinion, to the extent that our country is subjected to or willing to be affected by that—I do not think that Kim Jong-Un really cares that much—and the denial of aid or trade and/or something that we have used as an increasingly effective tool, which is financial sanctions to the most significant economy and financial system in the world.

And so when we do not want to engage militarily, this is the universe that we have in peaceful diplomacy engagement. So I do not believe it is a sword to take out all the time, but I do believe that in certain cases it is incredibly important.

In the case of Russia, they have violated the international order by invading and occupying sovereign countries, interfering in elections across the globe to sow distrust in the foundations of democracy, including here in the United States, and oppressing their own citizens. And if we want to ultimately have Russia and send a global message that there are going to be consequences for violating the international order and to send it not just in Russia's case but in the case of others who may consider violating the international order, it is sanctions that very often can be the tool.

I particularly get concerned about Russia not only interfering in our elections but violating arms treaties, which has lost some attention but is incredibly important. So I was pleased to join my colleagues in sponsoring the Countering Russian Hostilities Act. Like anything, it can be perfected, but I think it is a way forward.

So I want to ask our witnesses, I know that some of you have talked about the reticence of sanctions use and getting our partners, particularly Europeans, on board. But isn't it true that when we started the sanctions on Iran, we did not have European partners on board at the beginning. We brought them on board. There are times in which the United States must lead, and in leading, it then creates an international coalition. Isn't that a fair statement? Any one of you want to answer?

Ms. ROSENBERG. Yes, certainly. Someone has to lead and this body has in the past very effectively.

Senator MENENDEZ. And if we waited for a coalition to take place first before we led, we would not have brought Iran to the negotiating table as we subsequently did. So I get concerned sometimes when I hear about that we will have reticence from our partners. Our partners very often will have reticence, but it is when we lead that we ultimately—and it is a robust diplomacy that is necessary to assure that and to show them why it is in their interest as well.

Do you believe that among your discussion—which I have read your testimony and got a synthesis of what you said—is that having targets—do you believe, for example, that the violation of the Intermediate-Range Nuclear Forces Treaty that Russia recently conducted a violation of by deploying a ground launched cruise missile system, do you believe that sanctions play a role in ensuring,

for example, Russia complies with international arms control treaty obligations?

Ms. ROSENBERG. Sanctions have not traditionally been a tool used to address that kind of violation, and as was demonstrated by the previous U.S. administration. There are other messages of diplomacy or engagement that have been a first step toward addressing and disclosing those, and working toward a remediation of them.

I would offer that I think that kind of diplomatic and direct engagement and disclosure is a first, most important step and would reserve the option to consider sanctions, but not as a first step.

Senator MENENDEZ. Well, I hope that the Administration engages Russia on its violation of that treaty. That to me is one of the most significant violations that have taken place that are a real consequence to U.S. national interest and security, as well as, of course, what they have done here in the cyber attack against our own democracy. I consider that an attack against the United States, one that, if it was in any other dimension, we would be responding to vigorously. And we seem not to have been engaged in responding to it vigorously, and I hope that we look at sanctions, the perfecting of sanctions in that regard.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you.

Senator Kennedy.

Senator KENNEDY. Thank you, Mr. Chairman.

Mr. Lorber, do you believe the current sanctions against Russia have had any meaningful impact on Mr. Putin's behavior?

Mr. LORBER. Yes, Senator, I do. I think that there are multiple indications of this impact. The first element of this impact is from a deterrence perspective. So there were indications, so I have been told, that Russia was persistent to engage in even more aggressive activity in 2014, and they stopped short because of the fear of sanctions.

Senator KENNEDY. Well, how do you know that? That is like saying let me tell you how many fish I did not catch on Saturday because I did not go fishing. You do not know that, do you?

Mr. LORBER. That is a fair—I do not know that for certain.

Senator KENNEDY. It did not stop Mr. Putin from—it did not stop his aggression in Syria, did it?

Mr. LORBER. No. We did not have sanctions on Russia in response to Syria, but that is correct. It did not stop his activities in Syria.

Senator KENNEDY. It did not stop him from trying to influence the American elections, did it?

Mr. LORBER. I do not know—I assume it did not, no.

Senator KENNEDY. It has not stopped him from implementing a disinformation campaign in countries in the European Union, has it?

Mr. LORBER. I think that is correct.

Senator KENNEDY. OK. What would be the most Draconian sanctions that the United States could impose upon Mr. Putin unilaterally?

Mr. LORBER. So the United States—I am not recommending to do this—

Senator KENNEDY. I understand. This is just information gathering.

Mr. LORBER. Yeah, sure. The United States could take a number of actions. It could basically shut off the Russian financial system from the U.S. financial system. It could order all of the U.S. banks to close correspondent accounts on behalf of Russian financial entities, which would very likely have the impact of crashing the Russian financial system.

Senator KENNEDY. Right. Now, you talked about—the three of you, any of you could answer this. I do not mean to pick on Mr. Lorber. You talked about Mr. Putin in response to Senator Sasse's questions and his net worth. He is only the tallest hog at the trough. There are others at the trough, right? Do we know where their assets are?

Mr. LORBER. We have some indications of where some of their assets are in the United States. That was information that has been developed through FinCEN, through one of their geographic targeting orders. But we do not have a broad understanding of where their assets are.

Senator KENNEDY. But you know where some of them are.

Mr. LORBER. We have been told that there is information suggesting that a lot of their assets are New York and San Antonio and Miami and San Francisco real estate properties.

Senator KENNEDY. And you know where some of Mr. Putin's assets are, do you not? Ms. Rosenberg, did you not say we could trace some of their assets to real estate in Europe and in the United States?

Ms. ROSENBERG. Well, that may have been Mr. Lorber's comment, but I would agree that there is a broad perception, backed up by certain evidence disclosed by the geographic targeting order from FinCEN indicating that Russian elite assets, not specifically Mr. Putin's, which—

Senator KENNEDY. Do you know where Mr. Putin's assets are, some of them?

Ms. ROSENBERG. I do not know—

Senator KENNEDY. Do you think anybody does?

Ms. ROSENBERG. Yes, I think someone does.

Senator KENNEDY. OK. What would happen if we froze his assets and those of his participants in the crony capitalism?

Ms. ROSENBERG. That I am not sure is—that seems to me a very challenging proposition, in part because—

Senator KENNEDY. Let us assume for a second we could do it. What would be the consequences of that in terms of the global economy? And in answering that, what percentage of the world gross national product is the Russian economy?

Ms. ROSENBERG. I can speak to the first one first. So if we are thinking about this hypothetical situation, the assets of President Putin and his close associates, what may be beneficially owned by them directly as well as indirectly, are talking about a massive amount of money. If it were possible to go after that, I think there would be profound collateral consequences across the global economy and certainly in the United States. This is—

Senator KENNEDY. He owns assets of that size that would affect the global economy if they were frozen?

Ms. ROSENBERG. What I said was his assets, both direct beneficial ownership as well as indirect beneficial ownership, and those of his associates.

Senator KENNEDY. Well, what would be the collateral consequences other than changing his behavior?

Ms. ROSENBERG. Well, I will set aside changing his behavior, but as far as the economic consequences, I think it would be profound probably for all large U.S. global banks which would be in the position of implementing such a sanction. It would be a compliance and liability nightmare for them, as well as—

Senator KENNEDY. I have got 6 more seconds, so I have to interrupt you. We have just been nibbling around the edges here. The man is, your testimony is, worth tens of billions of dollars. Time Magazine says he is the most powerful man in the world. You cannot seriously believe that nibbling around the edges is going to change his behavior; we either put sanctions on or not.

I went over. I am sorry, Mr. Chairman.

Chairman CRAPO. Thank you.

Senator Warren.

Senator WARREN. Thank you, Mr. Chairman. And thank you all for being here today.

Our intelligence community has determined that Russia engaged in cyber attacks on the United States to interfere with our election, and several members of the Trump administration and campaign have questionable ties to Russia. There is good reason to believe that President Trump himself has substantial financial ties to Russia, only we do not know the details because he will not release his tax returns.

None of this is normal. We are not even 2 months into the Trump administration, and FBI counterintelligence investigations and congressional inquiries have already been launched. Senior officials were caught lying to Congress. A national security adviser resigned in disgrace because he misled White House officials and the FBI about his Russian ties. And in the middle of all of this, Donald Trump incredibly continues to consider lifting sanctions against Russia.

Now, last week, a Senate Subcommittee held a hearing with Ambassadors from six European countries—Ukraine, Poland, Georgia, Latvia, Lithuania, and Estonia. Four of these countries are members of the European and the NATO Alliance. They are all American partners living on the front lines of Russia's destabilizing influences.

At this hearing the Ambassadors agreed that the United States should not ease sanctions on Russia unless Putin actually makes some changes. So let me start there.

Ms. Rosenberg, if we ignore our allies and ease sanctions without meaningful changes in Russia's behavior, does that increase or decrease Putin's ability to destabilize countries along its border, in the rest of Europe, and around the world?

Ms. ROSENBERG. Certainly that would increase it. Russia thrives in that kind of environment. With its information campaigns and its destabilization conducted through information and funding of political parties, we would throw our European allies under the



bus. It would be difficult and damaging to transatlantic unity, which is challenging for the pursuit of our national interests.

Senator WARREN. Yeah, and let us start with that basic principle that the purpose of sanctions is to discourage and change bad behavior. If Russia stands firm and we drop our sanctions in exchange for nothing, we are just weak. So sanctions work better, as you note, when we coordinate with our allies and our partners. Right now, the United States and the European Union coordinate sanctions on Russia's financial, energy, and defense industries for invading Ukraine's territory and undermining its sovereignty. These sanctions have taken a toll on Russia's economy. The EU sanctions must be renewed every 6 months, and they did just that, renewing them now until the end of July.

Ms. Rosenberg, is it fair to say that it is not easy for the European Union to keep doing this given the close economic ties between Europe and Russia?

Ms. ROSENBERG. Yes, I think that is fair to say and particularly for some more economically exposed countries than others.

Senator WARREN. And yet they keep doing it. Why?

Ms. ROSENBERG. For a variety of reasons. I would suggest that they value their unity with the United States and the messaging effect that this has. They want to send a clear signal about what it means to violate Ukrainian sovereignty. And notwithstanding the economic pain for them, they still believe that this project and the self-sacrifice economically is worth it for the political and strategic benefit they may gain.

Senator WARREN. And I understand from what you are saying here that one of our strongest tools against Russia is joint EU-U.S. economic pressure, that this is much stronger if we are working together. But if the United States unilaterally lifts its sanctions on Russia, which, of course, then encourages the European Union to do the same, how effective will U.S. and European efforts be to hold Russia accountable?

Ms. ROSENBERG. Well, it may be very difficult to reestablish a united transatlantic front with economic measures toward Russia, particularly given the nationalist political currents that are more prominent now than they were in 2014. So that is one primary problem that will be an impediment.

Also, I would suggest that the United States and the European Union will lack credibility if they try and do this again because we look fickle if we impose and then remove, particularly with no behavior change on the part of Russia.

Senator WARREN. Fickle and weak. Congress must be able to review any attempts by this President to roll back our sanctions against Russia. I have cosponsored legislation that would do just that. We still do not know what is going on with this Administration's ties to Russia, but as we wait for the facts to come out, strong congressional oversight is needed to ensure that the President does not throw away our leverage against Russia for nothing. Thank you.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator  
Senator Tillis.

Senator TILLIS. Thank you, Mr. Chair. Thank you all for being here.

First and foremost, I think it is an absurd notion to think that this Administration would act unilaterally to ease sanctions on Russia knowing what this President knows now. So that is great for talking points, great for the midnight news cycle, but not a practical reality. This body would probably vote unanimously against any of that activity, so we need to make it very clear that is not on the table, except for the political rhetoric.

And my answer to Senator Sasse's question is Putin is as rich as he wanted to be. He is a totalitarian dictator who is putting the lives of 140 million-plus Russians at risk in terms of them being able to feed themselves and live a secure existence.

What I think we need to talk about—look, I am all for projection of U.S. might, but I happen to agree right now that Vladimir Putin is probably the most powerful man in the world. He does not happen to lead the most powerful nation, but either legally or illegally, he can bring weapons to bear and devices to bear that the United States would not. And so we have to recognize him for what he is.

But by the same token, we should not take the bait and overreact at the expense of hopefully winning the hearts and minds of the Russian people. Right now, the Russian people—you know, it is kind of difficult to figure out in the mind of somebody who you call up and ask what is your opinion of Vladimir Putin if you live in Russia. You are probably inclined to say you like him whether you do or not. But the reality is he is polling at 80 or 83 percent in terms of public opinion. So if we attack Putin and, I think, to use your words, Mr. Lorber, our response is too powerful, it could be at the expense of ultimately achieving what we want to achieve.

So my question to you all is: What would be a more exquisite, more sustaining regimen of sanctions that—you know, we can talk about the money laundering, we can talk about their weapons laundering. We can talk about any number of manipulative practices that either Putin knew about or should have known about. We can talk about their sovereign incursions and everything else. But have you all thought about like an idealized framework, a multilateral engagement with the EU or NATO partners, what you would consider to be an idealized framework to really get to a point where you do not harm the individuals in Russia who are really, I think, peaceful people that we would like to develop a good relationship with, but these greedy, lawless leaders at the top, what sorts of regimens could we put into place that would make them start producing a better behavior that is to our mutual best interest? And in that, we talk about energy policy relating to sanctions making it harder for them to extract and distribute their natural gas in particular because there is a heavy reliance in Europe, and I understand that and the effect that it would have on our partners, which would make them apprehensive about going that direction. But I do believe U.S. energy policy can play a very important role in providing European nations with a choice that will make them have more options as we have to move forward and ratchet up sanctions.

So in my remaining time, if you can give us an idea of—let us cut the politics out of this, let us get to a good, sustainable place

in sanctions—what does that look like from an idealized perspective, your idealized perspective? We will just go down the line.

Thank you, Mr. Chair.

Ms. ROSENBERG. Thank you for the question. I think this is a really important question to think about the framework and the strategy for an incremental and sustainable imposition of sanctions, escalation of sanctions.

I would offer two principles right at the beginning, and the first is that sanctions should not be the only policy tool used to increase pressure on Russia; and, furthermore, that in addition to pressure on Russia economically, I would suggest and urge a corresponding outreach to the people of Russia to try and counteract along the lines that have been used in other sanctions programs, people-to-people exchanges, encouraging that to counteract the narrative that will be prominent in Russia, even more prominent than it is now, that these sanctions are meant to punish and penalize the Russian people.

The first best step for enforcing and strengthening these sanctions is to further enforce sanctions already in place, authorities already on the books, and there is plenty of scope within the existing authorities. So in your capacity of oversight of the Administration, urging them to do things like add additional entities or sectors to the SSI list, further restrict new kinds of financial products that are restricted for those entities on the SSI list, and adding more names, that will all have an economic effect and a strong signaling and deterrence effect, and that is an area, apropos of Senator Menendez's question, where the United States can and should lead partners who can and should do that in addition. There are opportunities there for Europe along with the United States. After that is a good opportunity for new sanctions authorities, as are being considered in the Senate and the House right now.

Chairman CRAPO. Our time has expired, and we are going to be really tight getting through all of our Senators, so if the remaining two witnesses have anything to add, you could briefly do so, please.

Senator TILLIS. Actually, I would prefer just to defer, and if you would contact my office, this is particularly important to me. I sit on Senate Armed Services, so I would like this feedback. I would like to act on this, not just hear your comments and wait for the next hearing.

Thank you, Mr. Chair.

Chairman CRAPO. Thank you, Senator.

Senator TESTER.

Senator TESTER. Yeah, thank you, Mr. Chairman, for holding this hearing, and to you, too, Ranking Member Brown. I think this is a critically important hearing. It is important for the American public and all of their elected representatives to remember this: Russia attacked the United States and sought to undermine our bureaucracy. It is not a partisan issue. It is not something we should be playing politics with, though I am increasingly concerned that we may be heading in exactly that direction. We all took a solemn oath to this office to defend our Nation from foreign threats, and we must not lose sight of that duty.

Before I talk about the sanctions, I want to talk about where this Nation and Congress is currently. We have become far too

politicized, which really threatens our national security, and I am troubled when I see respected voices like John McCain and Lindsey Graham, hear their voices fall on deaf ears of their leadership when they call for a bipartisan, transparent investigation into Russia's action. I am troubled when the American people are stonewalled from learning more about the connections between Trump's team and Russia. Just this past week, we had a close associate admitting that he communicated privately—a Trump close associate admitting that he communicated privately with a hacker who was believed to be a front for the Russian military. Before that, General Flynn lost his job for misleading the Vice President of the United States over the contents of conversations that he had with the Russian ambassador.

Americans deserve an independent, transparent view of these types of relationships, and that will strengthen our democracy. Failure to do so would play into the hands of nations like Russia and Putin, who seek to do us harm.

I believe that the sanctions that are in place in response to Russia's attacks on our democracy and aggression in Ukraine are a starting point, but I believe more needs to be done.

I will cut right to the chase. We have put sanctions on a lot of different folks out there. I need to know from the folks here—and I thank you for being here, by the way—your opinion on what would be the impacts if we sanctioned Putin. How would that be viewed? Anybody can jump in on that.

Ms. ROSENBERG. I think that would be an incredibly aggressive step, particularly as a next step. And as I was suggesting in my previous comments, I think there is a range of appropriate steps that could and should be considered before then.

There are very powerful implications of going after a head of state in this way that I think may not be the next step amongst the variety of tools that Congress should consider.

Senator TESTER. And before we get to you, you have laid out your steps—you do not have to do it again, but you have laid out the steps that this Committee should be looking at?

Ms. ROSENBERG. I have laid out a number of them in my testimony and would be happy to discuss them further.

Senator TESTER. OK. Go ahead.

Mr. LORBER. I agree with Ms. Rosenberg's assessment. I think it would be a very aggressive action that might not have economic effect on Vladimir Putin, but certainly would send a very strong, and perhaps too strong, diplomatic signal.

Senator TESTER. OK. Good.

Mr. LUDEMA. I think that, putting aside the wisdom of taking such an action from a political point of view, the economic effect of doing that would be—according to our research, would probably be quite negative for Mr. Putin and probably would not have a substantial economic effect on the United States or the European Union.

Senator TESTER. OK. Could you just quickly go through—and then I will give up the rest of my time—the steps you think we need to be considering, Elizabeth?

Ms. ROSENBERG. I would offer that the first of those would include encouraging the Administration to enforce—as well as EU

counterparts—existing sanctions further. That may mean adding new entities——

Senator TESTER. OK.

Ms. ROSENBERG.—or sectors to the SSI list, restricting different kinds of financial services that are——

Senator TESTER. OK.

Ms. ROSENBERG. Right. And then perhaps additional authorities, some of which have been discussed or proposed in legislation before the Congress right now having to do with financial services and energy.

Senator TESTER. OK. Thank you very much.

Thank you, Mr. Chairman.

Chairman CRAPO. Thank you, Senator.

Senator Heitkamp.

Senator HEITKAMP. Thank you, Mr. Chairman.

You know billions and billions of dollars, if you were just into this for money, you would take the money and go someplace else. Obviously, this accumulation of Putin's is really related to power and continuing and maintaining power. And, obviously, what you get from this Committee and the discussion that we are having today is that sanctions on Russia do not necessarily curb behavior when someone is accumulating enough power that he can, in fact, continue to behave with impunity on the world stage in ways that all of us should find reprehensible, including the absolutely brazen attacks on our electoral system.

And so we continue to be concerned about the amount of power that Putin has accumulated, especially given that he has made this seemingly in the interest of the Russian people. It makes this really complicated on how you deal with changing his behavior.

There are two things I want to talk about. Number one is this sense that if we cooperate with Russia, if we turn the page and have a different relationship with Russia, Russia will be on the same page in the fight against ISIS. That was one of the expressed theories of this Administration going forward. I would like to hear your comments on whether you think that is a wise course, even assuming that we have the same interest as it relates to ISIS.

Mr. LORBER. Do you mind if I take that first? So putting aside whether or not Russia would be a good partner in the fight against ISIS, which I know there is a lot of debate about, I still think it would be a mistake to trade sanctions for cooperation in the fight against ISIS, in large part because that would signal to Russia—for example, if we said, “Well, you know what? We are going to drop sanctions against Crimea that we have imposed,” it would signal to Russia that they can go ahead and continue their types of destabilizing activities in Eastern Europe, and it would also signal frankly to the rest of the world that principles of international law such as sovereignty are not as important to the United States as are other potential norms.

Ms. ROSENBERG. If I could add to that, I think it is important to bear in mind that the bilateral relationship we are talking about with the United States and Russia is very broad. It, of course, includes a variety of different files even in just the security domain. It is completely feasible to envision a relationship with Russia that may involve some element of cooperation or coordination in,

perhaps, the Syria file where there could be some kind of transactional politics and agreement, and simultaneously envisioning in, for example, the Ukraine file a maintenance of current sanctions and a relationship of pressure. That was the case with Russia in the last Administration, for example, when we saw the amplification of Russia sanctions while seeing simultaneously coordination with Russia on the Iran file to remove sanctions. I think that principle of a variegated relationship is one we should hold forefront.

Senator HEITKAMP. We have spent a lot of time talking about the European Union. We have not looked much into Asia and the relationship that Putin has with China, that Russia has with China, and the opportunity that he sees right now with the Arctic opening up and the challenges that we have in the Arctic. I would like just a quick—I only have about a minute left, but anyone who feels comfortable talking about how we need to engage with China in this discussion and also what opening up the Arctic has meant to his potential expansion on energy.

Ms. ROSENBERG. Speaking to the Russia-China relationship, this is one in which Russia is the junior partner to China, which has been very aggressive with Russia in its contractual demands for energy, for example. It has not, as some feared it might, been the backfill for European and U.S. sanctions, providing lots of capital where it was not available from the United States and European Union.

Senator HEITKAMP. We want China to continue to drive really hard bargains.

Ms. ROSENBERG. And for that reason, this Administration and Congress should set a tone of communication with China rather than antagonism in order for China to continue to set those hard bargains.

Senator HEITKAMP. I am out of time, and I want to respect the Chairman's desire that this move along. But I did want to maybe follow up with you on the Arctic question. I think it is critical.

Chairman CRAPO. Thank you, Senator.

Mr. LUDEMA. Can I just give a quick answer on that one? I think the ability of the Russian energy companies to take advantage of the Arctic is already being severely limited by the existing SSI sanctions because that is precisely the technologies that are being restricted.

Senator HEITKAMP. Thank you.

Chairman CRAPO. Thank you.

Senator DONNELLY.

Senator DONNELLY. Thank you, Mr. Chairman. I think that weakening sanctions against Russia is like saying that we support their invasion and occupation of Crimea, of Eastern Ukraine, of their actions in Syria, of their destabilizing Eastern Europe, of their attack on our election system and our country, and their cyber attacks as well. And so I think to even discuss that is astonishing to me for any Government officials to be talking like that.

Mr. Lorber, the question I wanted to ask you is that you noted in your testimony the fact that large sums of Russian money have been flowing into U.S. real estate markets. Russian oligarchs close to Putin are likely laundering funds through a network of shell

companies and depositing them in the United States through real estate investments.

How can we work with the Financial Crimes Enforcement Network to discover these suspect investments and to better find them and to seize them?

Mr. LORBER. Thanks, Senator. So the Financial Crimes Enforcement, or FinCEN, has over the past 2 years established geographic targeting orders which track cash payments or cash purchases of high-end real estate in a variety of markets, and that has provided FinCEN with information as to who is actually making these purchases. And often in cases it has turned out apparently to be Russian oligarchs. That is kind of the first step, which would be not only identifying that information but then having FinCEN work with the Department of Justice and with OFAC to identify who those individuals are, if any of those individuals are sanctioned entities, sanctioned persons, to seize those funds——

Senator DONNELLY. Have any of these real estate purchases been seized here in the United States?

Mr. LORBER. Not to my knowledge, but I——

Senator DONNELLY. So why would they be hesitant to continue to launder their money through this if zero have been seized at this time?

Mr. LORBER. So I do not have particular knowledge of where FinCEN is in terms of the information that they already have. If I had to guess, it would probably be to say that they are developing cases against particular individuals. But I do not know that.

Senator DONNELLY. I think a very cursory effort could provide them with about 100 quick targets throughout the United States, don't you? I mean, you know, the joke in New York is all you have to do is walk through Midtown at night, and you can see all of the luxury developments where, you know, floor after floor after floor are completely dark.

Mr. LORBER. I agree. I think that these targets are sort of low-hanging fruit or ones that we probably have readily available to us to be the subject of enforcement.

Senator DONNELLY. So what do we have to do to get FinCEN to move on these?

Mr. LORBER. Again, I do not know where FinCEN is specifically in terms of this process. They could be just at the cusp of going after them, though.

Senator DONNELLY. Well, my next question is: There are public reports indicating that the FBI may be investigating in one way or another Alpha Bank, which is a Russian bank. My understanding is Alpha Bank and its key stakeholders are not on the U.S. or EU sanctions list. Is that correct? That is for any of you.

Mr. LORBER. I do not know off the top of my head. I can run their names through the SDN list and come back to you with an answer.

Senator DONNELLY. OK. Elizabeth?

Ms. ROSENBERG. I believe that is correct.

Senator DONNELLY. OK. Are any of you familiar enough with Alpha Bank to assess its relationship to the Russian Government and to the network of oligarchs tied to Putin?

Mr. LORBER. Unfortunately, I am not, no.

Senator DONNELLY. OK. It seems the most effective sanctions are the ones against the financial sector. I mean, that is just what it seems to me. What can we do to make those sanctions against the financial sector more effective? If you had one suggestion—I just have a minute to go—I would love to hear each of your suggestions about what we can do to make financial sector sanctions more effective. You each have 20 seconds.

Ms. ROSENBERG. Broadly expand the entities targeted by SSI sanctions and certain of the financial products restricted to them.

Mr. LORBER. Increase the OFAC and relevant European Union and EU member state enforcement authorities so that they clamp down and make sure that no sanctions violations are occurring.

Mr. LUDEMA. Well, you could ban holding of existing paper rather than just new issues of paper.

Senator DONNELLY. OK. Thank you all, and I just want to say one other thing, Mr. Chairman. I want to thank Adam Szubin for his service to this country over the years. He did an extraordinary job at great sacrifice to his family, and we are much safer and better off because of his efforts.

Chairman CRAPO. Thank you, Senator.

Senator Van Hollen.

Senator VAN HOLLEN. Thank you, Mr. Chairman. I want to thank all the witnesses. My State of Maryland is home to the U.S. Cyber Command, and I think we all know that cyber attacks, cyber warfare, cyber interference is sort of the new dimension of international conflict. So I just have a few questions with respect to how we can use sanctions to deter that kind of interference. We see it, of course, on the commercial side as well as on the political side.

On the commercial side, my understanding is that the Department of Justice actually just announced that it is going to indict two Russian Government officers for the cyber hacking, wire fraud, and trade secret theft regarding Yahoo's breach of about 500 email accounts. That has obviously been an ongoing investigation. Under President Obama, we also had the sanctions targeted against certain Chinese individuals who were engaged in cyber theft.

But I want to just focus for a second on using sanctions with respect to cyber interference for political purposes. We have all talked about how the Russians interfered in our elections. There is no dispute about that. They use cyber, they use fake news. They did it to support Donald Trump's candidacy. That is the unanimous verdict of our intelligence agencies. And we also know they are doing it on an ongoing basis to interfere in the elections of our European allies—France, Germany—and we are going to get the results later today of the Netherlands elections. And they are doing it for the purpose of trying to undermine cohesion in the NATO Alliance, trying to undermine the European Union, because they want to encourage these nationalist sentiments that try to disrupt the unity that has been the cornerstone of our defense and our economic relationship. So we know what their strategy is.

My question is—and I could not agree more with my colleagues that not only should we make sure we pass legislation to prevent the rolling back of any sanctions currently in place by the United States and others, but I think we also need to join with our



European partners to respond with sanctions to the interference in our elections, these cyber attacks.

My question for all of you is: What do you think the appetite of our allies would be to ratcheting up sanctions against Russia specifically for their interference in our elections through cyber attacks and interference and hacking? And how would we best go about doing that, persuading our European partners that it is in our collective security and economic interest to do that?

Ms. ROSENBERG. Thank you for the question. In answering this, I want to step back for a second and say I think that there would be appetite in Europe and here to use policy instruments to respond to malicious cyber activity. However, in the framework of cyber deterrence, I would suggest that these are still very early days, and the development of a broad strategic doctrine for cyber deterrence may take decades, as it did for nuclear deterrence during the cold war. And there are no set rules of the road or a concrete escalation ladder for deterrence. And once those are in place, there will be an opportunity to discuss in more specific terms which measures would be amenable or advisable for European colleagues as well as in the United States.

However, I would just say in this hybrid warfare, including cyber activity and others, there is certainly a place for sanctions amongst other tools.

Mr. LORBER. I agree with Ms. Rosenberg. I think the first step here is deciding for ourselves what the rules of the road are, and then once we have made that decision, then we target actors in a public way that we feel step outside those bounds. And the sanctions for cyber activity in many cases may not have as much of an economic pinch as they do sort of a symbolic deterrence effect. And so I think that making sure that we have established those rules first will send clear signals to our adversaries that this activity is outside the bounds of what we consider to be acceptable.

Mr. LUDEMA. We have already identified quite a number of cyber companies and individuals associated with the cyber attacks and singled them out for sanctions. I would say that we would need to continue to find them and continue to sanction them.

What our analysis shows is that when you impose blocking sanctions upon these individuals, it does have a significant effect and will degrade their ability to conduct further action.

Senator VAN HOLLEN. Thank you. I think that the prosecutions we brought against the Chinese actors certainly helped establish the U.S.-China cyber agreement. So I appreciate your testimony. I know time is limited, but I look forward to following up with you. Thanks.

Chairman CRAPO. Senator Cortez Masto.

Senator CORTEZ MASTO. Thank you. Thank you, Mr. Chair. I appreciate the opportunity to participate in this important discussion. Thank you to the panelists. I apologize for my tardiness. I have a competing Commerce Committee meeting going on at the same time. But thank you for the discussion, and I have had the opportunity to review your written testimony as well.

Let me turn to the G-7. As we all are aware, Russia was suspended from the G-8 after their incursion into Crimea in disregard for international law. Has Russia's suspension from the G-8 had

any meaningful impact on their economy, their security, or their influence? And I am going to open that up to the panel. And then along with that, what can the coalition of G-7 countries do to be most effective in influencing Russia to abide by international norms and the laws moving forward?

Ms. ROSENBERG. I can start. I think that it may be difficult to disaggregate the effect of removing Russia from the G-8 from other effects taken effectively and simultaneously, including sanctions, U.S. and EU sanctions, and a reinvigoration of NATO with respect to the Russia threat. However, I think that a primary effect of this removal had to do with signaling and the message that it sent to Russia and the global community about the interest of this group in holding to norms, particularly global norms, sovereignty, and what it means for Russia to no longer be welcome in that group of nations holding these norms.

Senator CORTEZ MASTO. Thank you.

Mr. LORBER. I agree. Thank you for your question. And I think that the primary thing that the G-8, now G-7 could do is offer as a carrot for Russia's reintegration in the case is that Russia fulfills its obligations laid out under Minsk or reduces its cyber activities, *et cetera*. So I think that is a very serious carrot that we can offer.

Senator CORTEZ MASTO. Thank you.

Mr. LUDEMA. Yeah, I would say that it was a political move and not an economic one. I do not think that there is a great deal of economic benefit *per se* to being part of the G-8 or G-7, despite the fact that it is an important body for coordinating economic policy.

Senator CORTEZ MASTO. No, and I agree, it is a symbolic move, like the hearing we are having today I think is a symbolic move that is important for the United States.

You have also discussed expanding sanctions or improving on the current sanctions regime in some way. And while there certainly must be repercussions for Moscow's actions and they cannot be allowed to act with impunity, how is this not just more of the same? In other words, what in Putin's behavior or in Russia's current standing makes you believe that this will produce any of the behavioral changes we are seeking from Moscow?

Ms. ROSENBERG. I do not think it is redundant to engage in the active reaffirmation of principles, particularly when political circumstances change, including in the United States and in Europe. So reaffirmation of the posture toward Russia and condemnation of its aggression and foreign adventurism has political and messaging merit, and it may have economic effect as well. So I see it more as a reaffirmation rather than redundancy.

Mr. LORBER. And I think there is some indication—as I was speaking about with Senator Kennedy, there is some indication that the sanctions have had an impact on Russian decisionmaking. So, for example, you see Vladimir Putin and Foreign Minister Lavrov coming out on fairly regular occasions saying, “We want to get the EU sanctions off of us; we want to get the U.S. sanctions off of us. They must be pulled down.” And so I do think to an extent it is impacting their choices.

Senator CORTEZ MASTO. OK.

Mr. LUDEMA. I would say that standing pat is not the same thing as standing still. The existing sanctions that we have, particularly

the SSI sanctions, will tighten over time as more companies roll over their debt, as the Russian energy companies are forced to move out of conventional drilling and into more exotic drilling. These things are going to slowly and systematically degrade the long-term growth prospects for the Russian economy. So I do not think that we should think that just because we have not imposed new sanctions up to this point that these sanctions are not going to have a continued effect.

Senator CORTEZ MASTO. Thank you. My time is running out, and I just want clarification on one thing you were talking about, Financial Crimes division, FinCEN. And as the Attorney General of Nevada, I had the opportunity to work with them. So let me just clarify. It was not that you were saying they were not taking action with whatever information they are gathering with respect to real estate purchase by Russian oligarchs, correct?

Mr. LORBER. That is correct.

Senator CORTEZ MASTO. You just do not know of the action.

Mr. LORBER. That is absolutely correct. I do not know what action they are taking, but I do not—

Senator CORTEZ MASTO. That does not mean they are not taking that action—

Mr. LORBER. That is correct.

Senator CORTEZ MASTO.—as a body that gathers that data and working with those law enforcement agencies, correct?

Mr. LORBER. That is correct, Senator.

Senator CORTEZ MASTO. Federal law enforcement. Thank you. I appreciate it. Thank you so much for the comments today.

Chairman CRAPO. Thank you very much, Senator. And I want to thank all of our Senators and our witnesses for following the time. We made it almost by 5 minutes to 12. We just ran over a little bit.

To our witnesses, I want to say thank you again also for coming. I do ask that you respond promptly to questions that you will receive from the Senators who have 7 days to submit follow-up questions to you. You have been very helpful to us.

When I hit the gavel, I am going to be heading out the door fast because I am already late to another meeting. But once again, we appreciate this. It is a critical issue, and we will be working together to try to move forward on making sure that we develop the right policy for this country.

This hearing is adjourned.

[Whereupon, at 12:01 p.m., the hearing was adjourned.]

[Prepared statements and responses to written questions supplied for the record follow:]



March 15, 2017

Testimony before the Senate Committee on Banking,  
Housing, and Urban Affairs  
Assessing U.S. Sanctions on Russia: Next Steps

Elizabeth Rosenberg, Senior Fellow and Director, Energy, Economics, and Security Program  
Center for a New American Security

Chairman Crapo, Ranking Member Brown, and distinguished members of the Committee, thank you for the opportunity to testify today on the topic of U.S. sanctions on Russia.

The sanctions that the United States and the European Union imposed on Russian entities and individuals over the last several years have been among the most innovative, targeted, and forceful examples of modern coercive economic statecraft. Designed to respond to Russia's illegal annexation of Crimea and aggression in Eastern Ukraine, the most powerful of these sanctions targeted Russia's financial services, energy, and arms sectors, as well as individuals close to President Vladimir Putin. These multilateral measures delivered a powerful message of transatlantic unity regarding Russia's breach of Ukrainian sovereignty and cultivated substantial economic leverage for the West. Their impact and leverage were significantly augmented by the oil price collapse in 2014 and Russia's resulting loss of hard currency to cope with the sanctions vice. Transatlantic leaders have linked implementation of the Minsk agreements, including a cessation of hostilities, withdrawal of heavy weapons from the front lines, restoration of Ukraine's borders, sovereignty, and political reform, to removal of sanctions.<sup>1</sup> Sanctions linked to Crimea can be removed when Russia returns control over the peninsula to Ukraine.<sup>2</sup> Additional recent U.S. and EU sanctions have exposed Russia's human rights record, its destabilizing involvement in the conflict in Syria, as well as its insidious cyber intrusions into U.S. institutions and political processes.

The economic force of these sanctions has diminished over time as investors have adapted their business operations, the Russian economy has stabilized, and U.S. and EU leaders have not kept up the pressure of sanctions. Now, political signals from the new U.S. administration, as well as from nationalist political movements in Europe that could impact upcoming elections and leadership in France and Germany, that a warmer relationship with Russia may be forthcoming indicate to the

<sup>1</sup> Andrea Thomas, "German Chancellor Merkel Says No Quick End to Sanctions Against Russia," *The Wall Street Journal*, October 23, 2015, <https://www.wsj.com/articles/german-chancellor-merkel-says-no-quick-end-to-sanctions-against-russia-1445611095>; "Package of Measures for the Implementation of the Minsk Agreements," February 12, 2015, accessed March 10, 2017, <http://www.elysee.fr/assets/Uploads/Package-of-Measures-for-the-Implementation-of-the-Minsk-Agreements.pdf>.

<sup>2</sup> Nikki Haley, "Remarks at a UN Security Council Briefing on Ukraine," (UN Security Council Briefing on Ukraine, New York, February 2, 2017), <https://usun.state.gov/remarks/7668>.

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**Innovative.**

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private sector that sanctions may present even less of an impediment going forward. The U.S. Congress is in the position to enhance pressure through new sanctions in response to Russia's increasing aggression in Eastern Ukraine, as well as its deeply concerning cyber interference in U.S. institutions and electoral processes. Congress can offer leadership on the direction for an updated economic response, and set the tone for appropriate diplomatic overtures to both European allies and Russian counterparts.

### The Effects of Russia Sanctions

The powerful economic effects of Western sanctions on Russia in 2014 are clear, and they have had an influence on Russia's foreign policy since that time. Financial sanctions<sup>3</sup> locked major Russian entities out of Western capital markets and forced a scramble for hard currency, and pressure on state savings, to quickly repay massive debts.<sup>4</sup> They compelled U.S. and European oil companies to pull back from frontier oil developments with Russian firms<sup>5</sup> and hampered Russia's access to military technology necessary to its broader security modernization efforts.<sup>6</sup>

The record of Russian economic performance over the last few years demonstrates a period of distress. From the beginning of 2014 to December 2016 Russian external debt shrank from \$729 billion to \$519 billion,<sup>7</sup> and officials drew down the Reserve Fund (one of the country's two sovereign wealth funds) from \$87 billion to \$16 billion.<sup>8</sup> In an effort to stabilize the economy Russian officials put in place a series of spending cuts, to take effect over the 2017-2019 period, in education (20 percent in real terms),<sup>9</sup> healthcare (25 percent in real terms)<sup>10</sup> and defense (17 percent in real terms).<sup>11</sup> Russian economic managers also allowed the ruble to plunge in value from 33.15 rubles per U.S. dollar at the beginning of 2014 to as low as 83.59 rubles per U.S. dollar in January

<sup>3</sup> Executive Order 13662 of March 20, 2014, Blocking Property of Additional Persons Contributing to the Situation in Ukraine, *Code of Federal Regulations* title 3 (2014): 16169-16171, [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo3.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo3.pdf). See Directives 1, 2, and 3 under Executive Order 13662.

<sup>4</sup> Simond De Galbert, "A Year of Sanctions Against Russia: A European Assessment of the Outcome and Future of Russia Sanctions," (Center for Strategic and International Studies: October 2015), [https://csis-prod.s3.amazonaws.com/s3fs-public/legacy\\_files/files/publication/150929\\_deGalbert\\_SanctionsRussia\\_Web.pdf](https://csis-prod.s3.amazonaws.com/s3fs-public/legacy_files/files/publication/150929_deGalbert_SanctionsRussia_Web.pdf), 7.

<sup>5</sup> *Ibid.*; See also Directive 4 under Executive Order 13662; Guy Chazan and Jack Farchy, "Russia Arctic Energy Ambitions Jeopardised by Western Sanctions," *Financial Times*, September 1, 2014, <https://www.ft.com/content/41d19b16-31e9-11e4-a19b-00144feabdc0>.

<sup>6</sup> Executive Order 13661 of March 16, 2014, Blocking Property of Additional Persons Contributing to the Situation in Ukraine, *Code of Federal Regulations* title 3 (2014): 15535-15538, [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo2.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo2.pdf).

<sup>7</sup> Central Bank of Russia, "Balance of Payments and Other Statistics Compiled under the Methodology of the 6th Edition of 'Balance of Payments and International Investment Position Manual' (BPM6)," *External Sector Statistics*, January 17, 2017, <http://www.cbr.ru/eng/statistics/?PrId=svs>.

<sup>8</sup> Ministry of Finance of the Russian Federation, "Key Figures of Reserve Fund Management," *Reserve Fund*, March 9, 2017, [http://old.minfin.ru/en/reservefund/statistics/res\\_key/](http://old.minfin.ru/en/reservefund/statistics/res_key/).

<sup>9</sup> "Russia's Reserve Fund Little Changed Over January," *Reuters*, February 2, 2017, <http://www.reuters.com/article/russia-funds-idUSR4N1CJ02C>.

<sup>10</sup> Andrey Movchan, "Pensions and Security: Russian Budget Reveals Government Priorities," *Carnegie Moscow Center*, December 15, 2016, <http://carnegie.ru/commentary/?fa=66454>.

<sup>11</sup> *Ibid.*

<sup>12</sup> Lucie Beraud-Sudreau and Douglas Barrie, "Russia's Defence Spending: The Impact of Economic Contraction," *Military Balance Blog (Posts from the IISS Defence and Military Analysis Programme)*, March 6, 2017, <http://www.iiiss.org/en/militarybalanceblog/blogsections/2017-edcc/march-f0a5/russias-defence-spending-7de6>.

2016.<sup>12</sup> Capital has fled Russia, roughly \$210 billion in 2014 and 2015 combined,<sup>13</sup> and GDP growth contracted from 0.7 percent in 2014 to negative 3.7 percent in 2015, and while it climbed back last year growth remained negative.<sup>14</sup>

Russian officials have acknowledged publicly that sanctions had an economic effect. President Putin stated in January 2016 that “sanctions are hurting us.”<sup>15</sup> Sanctions were a meaningful contributor to Russia’s agreement to the Minsk accord in September 2014 and the Minsk II revival in February 2015. Arguably, Russia refrained from more expansionist political and territorial aims because of Western sanctions pressure. Despite the ongoing and serious violence in Eastern Ukraine, Russia and separatists are not pushing deeper into Eastern Ukraine or seeking a potential land bridge to Crimea. During this time, however, under the cover of a retaliatory sanctions campaign, President Putin implemented an import-substitution program to prop up the Russian agricultural sector and decried Western economic attacks. His popularity grew from 61 percent prior to the conflict in Ukraine to 84 percent in February 2017.<sup>16</sup>

#### A Diminishing Economic Force

Over the last couple of years the effects of Russian sanctions have significantly diminished. This has been one important factor in the recent Russian economic stabilization. Cautious investors scared off by the sanctions are beginning to return and Russian firms have succeeded in bringing in financing that can be shifted to some of the state owned firms directly targeted by sanctions, a loophole in the sanctions on Russia. For example, the 2017 Eurobond issuances are expected to be almost triple the 2016 amount.<sup>17</sup> Also, in 2016, capital flight was the lowest since the financial crisis in 2008 and one tenth of the 2014 record.<sup>18</sup> Russian economic growth is expected to rebound to 1.1 percent growth in 2017,<sup>19</sup> and currency value has stabilized at 58.91 rubles per U.S. dollar.<sup>20</sup> Oil prices have risen roughly 108 percent from lows in January 2016,<sup>21</sup> and Russia has expanded its already massive energy output by 4.4 percent between January 2014 and January 2017, drawing in critical new revenue streams for state budgets.<sup>22</sup> In February 2017, Moody’s upgraded Russia’s outlook to “Stable” from the “Negative” rating it had given in April 2016.<sup>23</sup>

<sup>12</sup> “Exchange Rate Archives by Month,” (International Monetary Fund: March 9, 2017), [http://www.imf.org/external/np/fin/data/param\\_rms\\_mth.aspx](http://www.imf.org/external/np/fin/data/param_rms_mth.aspx).

<sup>13</sup> Leonid Bershidsky, “Deutsche Bank’s Russian Scheme Isn’t Needed in 2017,” *Bloomberg*, January 31, 2017, <https://www.bloomberg.com/view/articles/2017-01-31/deutsche-bank-s-russian-scheme-isn-t-needed-in-2017>.

<sup>14</sup> “Subdued Demand: Symptoms and Remedies,” *World Economic Outlook* (International Monetary Fund: October 2016), <http://www.imf.org/external/pubs/ft/weo/2016/02/#annex>.

<sup>15</sup> Kenneth Rapoza, “Putin Admits Sanctions Sapping Russia,” *Forbes*, October 21, 2016, <https://www.forbes.com/sites/kenrapoza/2016/10/21/putin-admits-sanctions-sapping-russia/#6505a76c25d4>.

<sup>16</sup> “Putin’s Approval Rating,” (Yuri Levada Analytical Center: February 2017), <http://www.levada.ru/en/>.

<sup>17</sup> Kira Zavyalova, “Stars Align for Russian Eurobond Issues After Three-Year Drought,” *Reuters*, February 21, 2017, <http://www.reuters.com/article/russia-eurobonds-idUSL8N1G61QS>.

<sup>18</sup> Bershidsky, “Deutsche Bank’s Russian Scheme Isn’t Needed in 2017.”

<sup>19</sup> “Subdued Demand” *World Economic Outlook*.

<sup>20</sup> As of March 3, 2017. “Exchange Rate Archives by Month.”

<sup>21</sup> U.S. Energy Information Agency (EIA), “Europe Brent Spot Price FOB,” March 3, 2017. Accessed March 13, 2017. <https://www.eia.gov/dnav/pet/hist/LeafHandler.ashx?n=PET&s=dbrte&f=D>.

<sup>22</sup> Ministry of Energy of Russian Federation, “Statistics,” Accessed March 9, 2017.

<http://minenergo.gov.ru/en/activity/statistic>.

<sup>23</sup> Amey Stone, “Moody’s Sees Russia’s Creditworthiness Stabilizing,” *Barrons*, February 17, 2017, <http://blogs.barrons.com/incomeinvesting/2017/02/17/moodys-sees-russias-creditworthiness-stabilizing/>.



Surely the Russian economy is not living up to its full potential, with property ownership rules and macroeconomic management at significant fault. However, the resilience and stabilization of the Russian economy confirms that recent impediments to investment and growth, specifically sanctions, are no longer cultivating truly difficult economic conditions. At present, they do not appear to be impeding plodding growth, and seem highly unlikely to compel President Putin to make any concessions to the West.

All sanctions programs will lose their force over time as economic actors find work-arounds and circumvention opportunities. Simply put, the leverage that sanctions generate is a perishable asset. If policymakers do nothing to alter or update sanctions, or enforcement authorities do not take actions against violations, the effects of sanctions will continue to diminish. In the Russia case, diminishing sanctions effectiveness redounds to the benefit of Russian economic and international business interests.

Broadly speaking, the reason for declining economic effects of the Russia sanctions is due primarily to a lack of their maintenance. U.S. and EU policymakers made only very limited efforts in this area in the last couple of years, significantly due to a lack of political will in Europe to craft and impose new sanctions.<sup>24</sup> European leaders have increasingly struggled over the last two years to hold the line on these sanctions, doubting their utility and advisability.

Since the U.S. presidential election, President Donald Trump's friendly stance toward President Putin has given rise to the perception that the United States will pull back from sanctions, or at least from their enforcement. President Trump has stated, "I would love to be able to get along with Russia."<sup>25</sup> For many, this indicates an impending removal of U.S. sanctions on Russia and the viability of signing new contracts with Russian firms. Upcoming elections in France and Germany in which Russia-friendly parties are making a strong showing also contribute to the perception that Russia will soon come in from the cold and sanctions will cease to be the threat they once were.<sup>26</sup> Additionally, the slow departure of the United Kingdom, Europe's major financial center, from the European Union signals to the business community the appearance of cracks in the common European foreign policy that hold economic sanctions in place.<sup>27</sup>

Russia is actively exposing and seeking to deepen these various fissures among transatlantic partners and pushing back against the weakening sanctions edifice. Through military posturing, media and cyber manipulation, and selected economic interventions, President Putin has been transparently engaged in a reproach of Western interests and unity. He has directed an aggressive role in Syria in

<sup>24</sup> Michael Bimbaum, "European leaders threaten new sanctions against Russia," *The Washington Post*, October 20, 2016, [https://www.washingtonpost.com/world/european-leaders-threaten-new-sanctions-against-russia/2016/10/20/ce5f8240-960e-11e6-9cae-2a3574e296a0\\_story.html?utm\\_term=.e9bfa9f279c0](https://www.washingtonpost.com/world/european-leaders-threaten-new-sanctions-against-russia/2016/10/20/ce5f8240-960e-11e6-9cae-2a3574e296a0_story.html?utm_term=.e9bfa9f279c0).

<sup>25</sup> Brian Naylor, "Nobody that I know of: Trump Denies Campaign Contacts with Russia," NPR, February 16, 2017, <http://www.npr.org/2017/02/16/515624391/nobody-that-i-know-of-trump-denies-campaign-contacts-with-russia>.

<sup>26</sup> Matthew Dalton, "France Poised for Pro-Russia Pivot," *The Wall Street Journal*, December 28, 2016, <https://www.wsj.com/articles/france-poised-for-pro-russia-pivot-1482946472>; Stefan Wagstyl, "German politics: Russia's next target?" *Financial Times*, January 29, 2017, <https://www.ft.com/content/31a5758c-e3d8-11e6-9645-c9357a75844a>.

<sup>27</sup> Laurence Norman, "Brexit Likely to Alter EU's Sanctions Policy," *The Wall Street Journal*, October 6, 2016, <https://www.wsj.com/articles/brexit-likely-to-alter-eus-sanctions-policy-1475726513>.

support of President Bashar al-Assad under the guise of counterterrorism. Russia has backed continued hostilities in Eastern Ukraine, which have ticked up recently, and in a newly provocative step has recently begun to recognize passports from the break-away Republics of Luhansk and Donetsk.<sup>28</sup> Russia is in ongoing violation of the Intermediate Range Nuclear Force Treaty, a cornerstone of post-Cold War nuclear arms control.<sup>29</sup> Russian airplanes recently buzzed a U.S. aircraft carrier in the Black Sea,<sup>30</sup> and they have approached the airspace of Japan<sup>31</sup> and allegedly violated the airspace of the Baltic states, all allies of the United States.<sup>32</sup> At the preeminent global energy forum last week in Houston, a massive Russian delegation boasted about lucrative and vast new opportunities for Western firms with Russia, the world's largest oil producer. Energy minister Alexander Novak told the industry "Russia is open, it is open to investment."<sup>33</sup> These projections of Russian force and the assertion of its economic strength clarify that Russia is a serious, if more limited, international competitor. The West increasingly will have to contend with Moscow to advance its security interests and leverage.

### Evaluating New Sanctions Choices

The new U.S. administration and Congress are now contemplating policy toward Russia, and how to handle sanctions measures as part of that policy. The White House has not yet charted a definitive path forward with the Kremlin or, for that matter, with European allies. Just before taking office President Trump suggested that a removal of sanctions is possible if Russia helps the United States to counter the Islamic State of Iraq and Syria (ISIS) and achieve other goals. He said: "if you get along and if Russia is really helping us, why would anybody have sanctions if somebody's doing some really great things?"<sup>34</sup> More recently, Secretary Tillerson has affirmed the administration's intent to hold the line on sanctions.<sup>35</sup> Members of Congress have met revelations by the U.S.

<sup>28</sup> "Eastern Ukraine witnessed 'most violent' week in over a year, says OSCE," *Deutsche Welle*, February 10, 2017, <http://www.dw.com/en/eastern-ukraine-witnessed-most-violent-week-in-over-a-year-says-osce/a-37502565>;

"Germany: 'Unacceptable' That Russia Accepts Separatist Ukraine Passports," *Deutsche Welle*, February 20, 2017, <http://www.dw.com/en/germany-unacceptable-that-russia-accepts-separatist-ukraine-passports/a-37638344>.

<sup>29</sup> Michael R. Gordon, "Russia Has Deployed Missile Barred by Treaty, U.S. General Tells Congress," *New York Times*, March 8, 2017, [https://www.nytimes.com/2017/03/08/us/politics/russia-inf-missile-treaty.html?\\_r=0](https://www.nytimes.com/2017/03/08/us/politics/russia-inf-missile-treaty.html?_r=0).

<sup>30</sup> Ivan Watson and Sebastian Shukla, "Russian Fighter Jets 'Buzz' US Warship in Black Sea, Photos Show," *CNN.com*, February 16, 2017, <http://www.cnn.com/2017/02/16/us/russia-us-ship-fly-by/>.

<sup>31</sup> Franz-Stefan Gady, "Japan Scrambles Fighter Jets to Intercept 3 Russian Strategic Bombers," *The Diplomat*, January 26, 2017, <http://thediplomat.com/2017/01/japan-scrambles-fighter-jets-to-intercept-3-russian-strategic-bombers/>.

<sup>32</sup> Damien Sharkov, "Russia Prompts 20 Nato Air Force Scrambles In Baltic," *Newsweek*, October 10, 2017, <http://www.newsweek.com/russia-prompts-20-nato-air-force-scrambles-baltic-508727>; Lisa Ferdinando, "Russian Airspace Violations in Nordic-Baltic Region Dangerous, Work Says," *DoD News*, October 7, 2017, <https://www.defense.gov/News/Article/Article/968780/russian-airspace-violations-in-nordic-baltic-region-dangerous-work-says>.

<sup>33</sup> Alexander Novak, "Russia's Energy Future," (CERAWeek, Houston, March 7, 2017).

<sup>34</sup> Peter Nicholas, Paul Beckett, and Gerald F. Seib, "Trump Open to Shift on Russia Sanctions, 'One China' Policy," *The Wall Street Journal*, January 13, 2017, <https://www.wsj.com/articles/donald-trump-sets-a-bar-for-russia-and-china-1484360380>.

<sup>35</sup> Carl Schreck, "Ukrainian FM Says Tillerson Pledges U.S. Support Against 'Russian Aggression,'" RFE/RL, March 7, 2017, <http://www.rferl.org/a/ukraine-says-us-tillerson-pledges-support-vs-russia-aggression/28356188.html>; "Minister of Foreign Affairs of Ukraine Pavlo Klimkin held a meeting with the U.S. Secretary of State Rex Tillerson," Ministry of Foreign Affairs of Ukraine, News, March 7, 2017, <http://mfa.gov.ua/en/press-center/news/55381-ministr-zakordonnih-sprav-ukrajini-pavlo-klimkin-proviv-zustrich-z-derzhavnim-sekretarem-ssha-reksom-tillersonomministr-zakordonnih-sprav-ukrajini-podyakuvav-za-solidarnisty-spoluchenh-shitativ-u-borotybi-ukrajini-proti-agresiji-rfposhlovna-praktichna-pi>.



intelligence community of Russian intrusion into the U.S. electoral process with alarm and critique. Many have indicated the intent to conduct a full investigation into these practices.<sup>36</sup> Members of the Senate have also proposed strong new sanctions on Russia<sup>37</sup> and an effort to prevent the U.S. administration from withdrawing sanctions without congressional approval.<sup>38</sup>

If U.S. policy leaders do decide to alter Russia policy, specifically by making changes to sanctions, the primary challenge will be creating a unified stance between Congress and the administration. If, for example, the U.S. Congress adopts tough new sanctions on Russia, over and against the wishes of the U.S. administration, it may ironically empower President Putin and create serious confusion in the business community. Private sector firms may be unconvinced that the Trump administration will enforce harsh new congressional sanctions. They will also face conflict of law problems as U.S. and EU sanctions move out of step, creating a complex web of potential liability. Cautious firms will hang back, and opportunistic entrepreneurs will move forward to sign deals with Russian firms. President Putin has demonstrated acumen leveraging this kind of confusion and disunity in Western political relationships to deflect attention and advance Russian interests.

Looking beyond this hypothetical scenario for Russia sanctions, there are two other likely policy courses that also would have the effect of empowering President Putin economically and strategically, at the expense of U.S. interests and transatlantic leverage. First, if transatlantic partners maintain status quo sanctions on Russia but neither update nor enforce them, the effects of sanctions will diminish further over time. The business community and Russian political leaders will infer a lack of commitment by the West. In this environment new business with sanctioned Russian firms will emerge, and Russian political leaders will perceive an opportunity to pursue foreign adventurism unchecked.

The second alternative policy course is one in which the U.S. administration unilaterally rolls back sanctions on Russia, perhaps as part of a deal with Moscow, signaling greater political leeway to President Putin in his international dealings. Appearing to appease President Putin in this way will suggest to him that his hybrid warfare approach, military posturing, direct interference in U.S. and other elections, and adventurism are acceptable. It could serve to encourage an escalation in such aggressive behavior, particularly on Russia's periphery. Additionally, it would constitute a truly historic signal from the new administration that interference in a U.S. presidential election will go unaddressed and invite our enemies to violate the sanctity of U.S. elections and our democracy openly and without restraint.

Moreover, unilaterally lifting U.S. sanctions will create a very difficult situation for allies in Europe. There may be some European articulations of concern about the current sanctions approach and its impact. However, there is no popular desire to capitulate to Russia, rescinding the demand that Russia implement the Minsk agreements and throwing out sanctions. European leaders prioritize and value their alliance with the United States and the international influence this confers. Without

<sup>36</sup> Austin Wright and Martin Matishak, "Senators set to huddle on Russia hacking probe," Politico, February 2, 2017, <https://www.politico.com/story/2017/02/russia-hacking-senate-investigation-234456>.

<sup>37</sup> U.S. Senate, *Counteracting Russian Hostilities Act of 2017*, S. 94, 115<sup>th</sup> Cong., 1<sup>st</sup> sess. <https://www.congress.gov/115/bills/s94/BILLS-115s94is.pdf>.

<sup>38</sup> U.S. Senate, *Russia Sanctions Review Act of 2017*, S. 341, 115<sup>th</sup> Cong., 1<sup>st</sup> sess. <https://www.congress.gov/115/bills/s341/BILLS-115s341is.pdf>.

U.S. sanctions on Russia they will scramble to push back on Russia and simultaneously maintain alliance with the United States. Countries on the European periphery, particularly the Baltic countries, will be left vulnerable by the abandonment of Washington on sanctions and the policy chaos that will ensue in Europe. The Lithuanian Ambassador to the United States praised the U.S. sanctions at a Senate hearing last week, calling them “the strongest tool we have in our toolbox,” and indicating that they “will unite Europe.”<sup>39</sup>

In the economic realm, unilaterally removing U.S. sanctions will create some confusion for the private sector, as U.S. sanctions move away from EU sanctions. This move will also create new commercial opportunities with Russia. The United States is a more aggressive enforcer of sanctions than Europe and is perceived to set a very strong bar on sanctions compliance. So, in the absence of U.S. sanctions and a clear signal from the U.S. administration that it is rejecting this economic check, the White House will be validating Russia’s message that it is open for business.

The only effective strategy for cogent and credible sanctions on Russia in the future is one in which the U.S. Congress and administration are at least loosely coordinated. Whether sanctions are expanded, or if they are pulled back, policymakers must coordinate signaling and clearly express legal expectations for the private sector. Moreover, a new direction for sanctions will be forceful if the sanctions are coordinated with European counterparts. Notwithstanding the previously mentioned political views in Europe and the United States that undermine, or call into question, common European foreign policy, NATO, and the transatlantic alliance, it is not impossible to envision a coordinated transatlantic policy emerging on Russia in the future. Ultimately, coordination between the U.S. Congress, the U.S. administration, and EU leaders on sanctions is essential for clarity of messaging and to prevent them from being, in practice, a sham policy effort rife with opportunities for circumvention.

#### The Role for Congress

Congress has an important role to play in the adaptation and management of future U.S. sanctions policy toward Russia. There is considerable expertise in this policymaking body on both the crafting of sanctions and the exercise of U.S. policy toward Russia. Congress plays a fundamental role in offering ideas for sanctions policy. It can also deepen the public conversation over the strategic basis and consequences of sanctions enforcement, or non-enforcement, for the United States and other stakeholders. Fundamentally, legislators have a powerful ability to signal policy imperatives to the U.S. administration, its allies in Europe, and in this case directly to President Putin and his associates, about the economic consequences of aggression and foreign adventurism.

More broadly on Russia policy, members of Congress are in a unique oversight position, capable of soliciting and making public expert views on the threats that Russia poses to U.S. institutions and core interests at home and abroad. Members of Congress working to set the right tone for U.S. engagement with Russia is crucial; they can be a source of important leadership in the overall execution of U.S. policy toward an aggressive adversary. Moreover, the decisions of Congress

<sup>39</sup> U.S. Congress, Senate, Committee on Appropriations, Subcommittee on State, Foreign Operations, and Related Programs, Hearing on Russian Policies & Intentions Toward Specific European Countries, 115th Cong., 1st sess., 2017, 230.

regarding appropriations and lawmakers' guidance on force posture and projection, and foreign assistance, is fundamental to advancing U.S. national security interests.

On Russia sanctions going forward, Congress can and should engage the administration to urge continued enforcement of sanctions and make clear the folly of any policy to remove sanctions without Russian fulfillment of Minsk commitments or cessation of malicious cyber intrusions. Congress must also ensure that outcomes of congressional investigations into Russian actions during the 2016 U.S. elections are factored into this discussion. Additionally, given the technical expertise of the Banking Committee in particular, members can offer a sober reminder to administration officials and colleagues in Congress of some of the core principles necessary to carry out a successful sanctions policy. There are four principles in particular to bear in mind with regard to Russia sanctions.

First among these is the necessity to maintain a broad coalition of support for the economic measures, for clarity of message and to prevent circumvention. This requires U.S. policy leaders to coordinate and move together with European allies, as previously mentioned. Second, sanctions cannot be the only foreign policy tool to use against Russia to advance U.S. interests in Ukraine, Syria, or with regard to Russian cyber intrusion. They must be accompanied by broad and intensive diplomatic engagement, a sustained commitment to NATO, and thoughtful use of U.S. foreign assistance and security assets abroad. When it comes to Ukraine, they must also be accompanied by transatlantic allies' provision of a serious package of economic, security, and technical assistance with specific conditionalities and assurances.

A third policymaking principle that is particularly important in the Russia sanctions case is the need to keep sanctions implementation consistently tied to specific foreign policy objectives. Decision makers cannot let them evolve into mere expressions of blunt hostility, punishment, or antagonism. Any new sanction must be accompanied by an articulation of the behavior change that U.S. leaders seek from Russia, and there must be a practical path laid out for relief from sanctions if Russia changes its behavior. If this is absent, sanctions cannot be the deterrent or inducement of behavior change that they are meant to be.

A final principle to guide Russia sanctions is that the development of new sanctions ideas, and their possible deployment, should not preclude a U.S. approach to Russia policy that can be both constructive and tough. It can feature sanctions on one policy issue area, such as Ukraine, but engagement and potential collaboration in another issue area, such as Syria and countering ISIS. The U.S.-Russian bilateral relationship is, of course, broad, featuring a variety of serious security interests. Over the last several years this relationship was able to accommodate strong coordination in the negotiation of the Iran nuclear deal and removal of sanctions, while simultaneously experiencing a sharp deterioration in relations due to Russian actions in Ukraine and the expansion of targeted sanctions on Russia. Going forward, the U.S. approach to sanctions can and must be as variegated as it has been in the past, featuring adaptation and tightening of sanctions in some areas, and possibly relief in others if policy circumstances merit.

#### **New Measures for Consideration**

Members of this Committee and other legislators in the Senate and House are considering a variety of approaches to maintain and deepen the effects of Russia sanctions. These include efforts to

compel the administration to hold the line on current Ukraine-linked sanctions; codifying existing executive sanctions authorities into law by statute; and urging enforcement of these executive authorities. These ideas have considerable scope and merit and should be seriously considered. In addition, newly proposed legislation to address Russia's malicious cyber activity would create new financial penalties for such action. Many legislators expect and demand a penalty for these intrusions and are looking expectantly to sanctions options. This is reason enough to carefully study and refine these new cyber sanctions ideas, along with additional cyber, intelligence, covert action, and other policy options, to expose and counter Russia's insidious cyber activities.

New sanctions proposals introduced in the Senate to deepen the penalties on Russia for its aggression in Ukraine would create aggressive new authorities to tighten Russia's access to financial services and its ability to garner investment in its vast oil and gas producing or pipeline delivery and export sector. These energy-focused measures could be tremendously damaging to markets, to U.S. credibility, and to the enterprise of U.S. economic statecraft more broadly.

Specifically, the aggressive new Russia energy sanctions currently under Senate consideration would be virtually impossible to implement, even with full European cooperation given the tremendous size and scope of the Russian energy and transportation sector. Europeans will not participate in such sanctions, even if they are inclined to strenuously expand economic pressure on Russia, given the disastrous economic consequences of, in effect, suddenly cutting off one of their most important sources of energy. U.S. lawmakers will look unserious if they impose policy that is impossible to implement. Even worse, it will undermine the ability of U.S. policymakers to use sanctions in any future instance because it will strengthen the impression of some that U.S. sanctions are a paper tiger lacking force and credibility.

Even if such sweeping energy sanctions could be implemented they would be deeply damaging to the economic interests of the United States and its allies. Russia is the largest oil producer<sup>40</sup> and the second largest producer of natural gas;<sup>41</sup> severely crippling this supply by halting foreign investment into its production and pipeline distribution would cause painful energy spikes and volatility that would ripple through the entire global economy. Any new energy sanctions on Russia should be the subject of serious discussion with European counterparts and U.S. economic managers.

There are other more targeted ways that U.S. policy leaders can expand financial and energy pressure on Russia if they determine that such steps are appropriate to address Russian threats. I believe this chamber is considering the idea of creating restrictions on the participation of U.S. individuals and institutions in the issuance of Russian sovereign debt, a powerful escalation in sanctions pressure. Legislators are also considering narrowing the access of Russian firms to U.S. capital markets by shrinking the maturity length of debt instruments, or access to derivatives trading, available to Russian firms. These ideas would make it significantly more difficult for Russian entities to raise money and access hard currency. They could be relatively targeted and implemented in an incremental fashion to minimize unintended consequences.

<sup>40</sup> Claudia Carpenter, "Russia Overtakes Saudi Arabia as World's Top Crude Oil Producer," Bloomberg, February 20, 2017, <https://www.bloomberg.com/news/articles/2017-02-20/russia-overtakes-saudi-arabia-as-world-s-largest-crude-producer>.

<sup>41</sup> U.S. Energy Information Administration, "Russia," last updated October 25, 2016, accessed March 10, 2017, <https://www.eia.gov/beta/international/analysis.cfm?iso=RUS>.



Other ideas that I believe this chamber is considering in the energy domain include the expansion of restrictions on U.S. firms from providing technology, equipment, and services to the Russian refining sector. Additionally, under consideration is the idea of expanding the shale, deepwater and Arctic restrictions in current sanctions to cover Russian oil ventures outside of Russia's territorial boundaries. These ideas would create some limitations on Russia's ability to upgrade its refining fleet to be able to deliver higher quality and higher value products for domestic use and export, primarily to Europe. It would also impose limitations on Russia's ability to launch frontier oil projects abroad in the future. In the current oil price environment, and given Russia's abundant untapped domestic crude resources, the new frontier oil measure would have no real immediate effect but would instead represent a clip on prospective energy developments and a symbolic gesture to limit Russia's international economic expansion.

Beyond these new sanctions ideas, Congress could lobby European leaders to expand economic pressure on Russia by toughening their own set of sanctions. European sanctions currently allow for some grandfathering of European business with Russia as well as some European financing for projects with Russia where such activities are not offered by U.S. entities. There may be opportunity for Europe to more closely circumscribe these permitted business arrangements. Congress should urge European counterparts to consider such options, while being cognizant of the broader economic burden European businesses shouldered when it comes to sanctions and their greater economic vulnerability to Russian retaliation.

These ideas, and others, are worth the careful consideration of the Congress. They can be measures to prepare for deployment, along with other policy options, to address Russian aggression and incursions in the future. They can also be a set of ideas to form the basis for discourse and negotiation between Congress and the administration to ultimately formulate a coordinated Russia policy. Additionally, they can be discussion points in a conversation with European allies about how to proceed on Russia policy. With a wide array of diplomatic relationships in Europe, foreign policy leaders in Congress can play a crucial role in this domain. As previously mentioned, any sanctions approach on Russia is stronger and more credible if it is coordinated between branches of the U.S. government and multilaterally, underpinned by close transatlantic communication and a clear-eyed appreciation of stakeholders' goals and challenges.

### Conclusion

The grave nature of U.S. security concerns at home and abroad regarding Russia means that the stakes are high for sanctions policy. Now, as U.S. leaders are contemplating recalibration of this policy they have less leverage than they did a couple of years ago and a much more challenging footing to keep transatlantic ties strong and respond to Russian aggression. The only path for continued effective sanctions on Russia is a difficult one. It involves negotiation and coordination among various leaders whose political and worldviews may render such activity distasteful and frustrating. Yet the alternatives, stasis or conflicting sanctions policy, delivers economic, security, and political benefits to President Putin and undermines U.S. interests. These are losing propositions. It is far preferable to maintain Western economic leverage with Russia and negotiate from a position of strength, whether or not an ultimate goal is a deal with the Kremlin. In this

context, U.S. leaders must pro-actively take on the project of updating sanctions and forging what will be a new stage in transatlantic coordination on this critical policy challenge.

## Biography

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Elizabeth Rosenberg is a Senior Fellow and Director of the Energy, Economics and Security Program at the Center for a New American Security. In this capacity, she publishes and speaks on the national security and foreign policy implications of energy market shifts and the environmental effects of climate change. She has testified before Congress on energy issues and been quoted widely by leading media outlets in the United States and Europe.

From May 2009 through September 2013, Ms. Rosenberg served as a Senior Advisor at the U.S. Department of the Treasury, to the Assistant Secretary for Terrorist Financing and Financial Crimes, and then to the Under Secretary for Terrorism and Financial Intelligence. In these senior roles she helped to develop and

implement financial and energy sanctions. Key initiatives she helped to oversee include the tightening of global sanctions on Iran, the launching of new, comprehensive sanctions against Libya and Syria and modification of Burma sanctions in step with normalization of diplomatic relations. She also helped to formulate anti-money laundering and counter-terrorist financing policy and oversee financial regulatory enforcement activities.

From 2005 to 2009 Ms. Rosenberg was an energy policy correspondent at Argus Media in Washington D.C., analyzing U.S and Middle Eastern energy policy, regulation and trading. She spoke and published extensively on OPEC, strategic reserves, energy sanctions and national security policy, oil and natural gas investment and production, and renewable fuels.

Ms. Rosenberg studied energy subsidy reform and Arabic during a 2004-2005 fellowship in Cairo, Egypt. She was an editor of the Arab Studies Journal from 2002-2005 and researched and wrote on Middle Eastern politics at the Council on Foreign Relations in 2003. She received an MA in Near Eastern Studies from New York University and a BA in Politics and Religion from Oberlin College.

CONGRESSIONAL TESTIMONY: FOUNDATION FOR DEFENSE OF DEMOCRACIES

Senate Banking, Housing and Urban Affairs Committee

# Assessing U.S. Sanctions on Russia: Next Steps

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The views expressed in this  
testimony are my own and  
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### Introduction

Chairman Crapo, Ranking Member Brown, and distinguished members of the Senate Committee on Banking, Housing & Urban Affairs, I am honored to appear before you today to discuss assessing U.S. sanctions on Russia and next steps.

I would like to focus my testimony on the effectiveness of the current U.S. sanctions programs targeting Russia, as well as what the United States can do to responsibly ramp up economic pressure on Russia to convince Moscow to cease destabilizing activities in Eastern Ukraine, reduce malicious cyber activities targeting the United States and its allies, and limit their military operations in Syria.

To date, U.S. sanctions on Russia have a mixed record of success. Many macroeconomic indicators and recent studies suggest the various forms of sanctions—in particular the sectoral sanctions imposed on key Russian economic sectors—have had an impact on overall Russian economic health. Likewise, Russian Government officials continually push for sanctions relief, either in public statements<sup>1</sup> or by trying to undermine EU sanctions,<sup>2</sup> suggesting that Russia is feeling the pinch.

Nevertheless, the United States has not achieved many of the core objectives it sought when deploying these tools; while the United States has imposed one of the most sophisticated sanctions regime ever constructed—including list-based sanctions targeting Russian individuals supporting separatist activities in eastern Ukraine, as well as individuals engaged in human rights abuses, a comprehensive embargo on Crimea, sectoral sanctions focused on key sectors of the Russian economy, sanctions targeting Russian malicious cyber activity, and secondary sanctions authority—Russia continues to engage in threatening activity in a range of areas. In Eastern Ukraine, Russian-backed forces continue to violate the ceasefire, routinely attacking Ukrainian villages and military personnel. Likewise, Moscow continues to target Russian opposition leaders, often with lethal means. Last year and again more recently, Russian opposition leader Vladimir Kara-Murza was poisoned after speaking out about Russian human rights abuses and corruption, with many believing the Russian Government was behind the attempt on his life.<sup>3</sup> This poisoning

<sup>1</sup> David Herszenhorn, "Putin Calls for End to Use of Sanctions and Criticizes U.S. in Afghanistan," *The New York Times*, July 10, 2015, <https://www.nytimes.com/2015/07/11/world/europe/putin-criticizes-us-role-in-afghanistan.html>; "Russia Can't Mend Times with U.S. While it Backs Sanctions: Lavrov," *Reuters*, Dec. 10, 2015, <http://www.reuters.com/article/us-russia-usa-lavrov-idUSKBN0T0YR20151210>; Roland Oliphant, "'Cancel Sanctions and Scale Back NATO' Russia Tells US as Vladimir Putin Scraps Nuclear Deal," *The Telegraph*, Oct. 3, 2016, <http://www.telegraph.co.uk/news/2016/10/03/putin-scraps-deal-to-dispose-of-bomb-grade-plutonium-in-swipe-at/>; "Russia Demands U.S. End Sanctions, Pay Compensation if Plutonium Accord to be Resumed: Draft Law," *Reuters*, Oct. 3, 2016, <http://www.reuters.com/article/us-russia-usa-nuclear-lawmaking-idUSKCN1231HA?l=0>.

<sup>2</sup> "Putin Steps Up Drive to Kill Sanctions Amid Signs of EU Disunity," *Voice of America News*, July 29, 2016, <http://www.voanews.com/a/putin-steps-up-drive-kill-sanctions-signs-eu-disunity/3440262.html>.

<sup>3</sup> Andrew Kramer, "More of Kremlin's Opponents Are Ending Up Dead," *The New York Times*, Aug. 20, 2016, <https://www.nytimes.com/2016/08/21/world/europe/moscow-kremlin-silence-critics-poison.html>.

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followed the shooting death of Russian opposition leader Boris Nemtsov in February 2015, a killing widely perceived as a response to Nemtsov's outspoken protests against the government.<sup>4</sup> In Syria, Russia continues to support President Bashar al-Assad with direct military intervention,<sup>5</sup> including during the Syrian Government's brutal assault on Aleppo.<sup>6</sup> And finally, in the cyber realm, according to the intelligence community, Russia has continued its efforts to influence and undermine U.S. allies across Europe, in recent months focusing these efforts on upcoming elections in Western Europe.<sup>7</sup>

This Committee should make no mistake; Russian activity in these areas poses a serious threat to U.S. interests and the United States should be prepared to use all elements of its national power—including its economic power—to blunt Moscow's ability to undermine U.S. interests at home and abroad.

Additional, responsibly crafted U.S. sanctions can be a powerful tool to impact Russia's decision making and reduce its nefarious activities in each of these areas. Specific types of sanctions that, if properly calibrated, could be particularly effective in increasing the pressure on Russia include:

- The codification of certain executive orders ("EOs"), including EOs 13660, 13661, 13662, 13685, and 13694, as well as additional statutory designations under these codified EOs;
- Establishment of a task force, potentially led by the Financial Crimes Enforcement Network ("FinCEN"), to identify and seize assets of targeted Russian persons, including those with close ties to Russian President Vladimir Putin;
- Certain restrictions related to U.S. and European financial institutions' purchase or facilitation of Russian sovereign debt, which has been a way for Russia to prop up Russian state-owned enterprises and financial institutions in the face of sectoral sanctions; and
- Primary and secondary sanctions on elements of Russia's oil and gas industry, with possible carve-outs for certain countries particularly dependent on the Russian energy sector.

However, any new sanctions on Russia must take into account four important considerations. First, while additional sanctions are appropriate here, Congress should be wary of imposing sanctions that are *too* powerful. If the United States attempts to impose broad, Iran-like sanctions on Russia that target large swaths of the Russian economy and do not contain carve-outs for allies and

<sup>4</sup> Andrew Kramer, "Boris Nemtsov, Putin Foe, Is Shot Dead in Shadow of Kremlin," *The New York Times*, Feb. 27, 2015, <https://www.nytimes.com/2015/02/28/world/europe/boris-nemtsov-russian-opposition-leader-is-shot-dead.html>.

<sup>5</sup> Sam Heller, "Russia in Charge in Syria: How Moscow Took Control of the Battlefield and Negotiating Table," *War On The Rocks*, June 28, 2016, <https://warontherocks.com/2016/06/russia-is-in-charge-in-syria-how-moscow-took-control-of-the-battlefield-and-negotiating-table/>.

<sup>6</sup> Alison Meuse, "U.N. Report Says Syrian Forces and Rebel Factions Committed Aleppo 'War Crimes'," *National Public Radio*, Mar. 3, 2017, <http://www.npr.org/sections/parallels/2017/03/03/518134951/u-n-report-says-syrian-forces-and-rebel-factions-committed-aleppo-war-crimes>.

<sup>7</sup> "Background to 'Assessing Russian Activities and Intentions in Recent US Elections': The Analytic Process and Cyber Incident Attribution," *Director of National Intelligence, Intelligence Community Assessment*, Jan. 6, 2017, [https://www.dni.gov/files/documents/ICA\\_2017\\_01.pdf](https://www.dni.gov/files/documents/ICA_2017_01.pdf).

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partners, this could backfire, limiting critical European willingness to participate in our sanctions campaign and making it more difficult for Moscow to fulfill—at least partially—U.S. demands. Similarly, such sanctions could do serious damage to the Russian economy in ways that threaten our interests; while we want to pressure Russia to cease its malign activities, destroying the Russian financial system or cratering its economy would have worldwide blowback, threatening markets across the globe.

Second, Congress should think through how it can unwind sanctions pressure in the case that Moscow—even partially—changes its behavior. Current sanctions bills, including the Countering Russian Hostilities Act of 2017 (“Countering Russian Hostilities Act”),<sup>8</sup> ramp up the pressure on Russia significantly. Yet, as we have learned over the past few years, unwinding sanctions can often be a difficult and fraught process, and Congress should think about how and when it will unwind sanctions even as it builds pressure. Any such new sanctions legislation should include built-in “off-ramps”—namely elements of the sanctions regime, such as specific designations or specific Directives—that could be undone in a situation of partial Russian compliance with its various obligations, such as those under the Minsk agreements. Such partial sanctions relief could be traded for Russian fulfillment of these obligations, and this approach would increase the chances the United States could limit—though not completely eliminate—Russian challenges to U.S. interests.

Third, any such sanctions must be nested in a larger strategy of pressuring Moscow, including aggressive diplomacy and responding in kind to malign Russian activities such as offensive cyber operations. Sanctions are a means to an end, and Congress and the administration must be clear as to what that end is and how they intend to achieve it. Ramping up economic pressure on Moscow without clear objectives, the employment of other coercive tools, and buy-in from the administration—is unlikely to be effective in getting Moscow to change its behavior.

Fourth and as I discuss below, the United States must be prepared to address Russian retaliation for such sanctions, including in the form of countersanctions, increased cyber attacks, and even kinetic action in ways that threaten U.S. interests.

I will focus my comments today on four main areas. First, I discuss the various elements of the U.S. sanctions program on Russia, including sanctions on Russia related to Ukraine, cyber activities, and corruption (together, the “U.S. Russia Sanctions Program”). Second, I discuss whether the U.S. Russia Sanctions Program has been effective, both in impacting the Russian economy and in changing Russian behavior in desired ways. Third, I discuss ways to further increase the pressure on Moscow in responsible ways, drawing in part on existing legislative proposals such as the Countering Russian Hostilities Act. Finally, I provide legislative suggestions to ensure that we are able to ramp down sanctions pressure when appropriate as effectively as we can ramp it up, increasing the likelihood that we will at least limit many of Moscow’s malign activities.

<sup>8</sup> S.94, “Countering Russian Hostilities Act of 2017,” 115<sup>th</sup> Cong. (2017).

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## I. Current U.S. Sanctions on Russia

Taken together, the current U.S. Russia Sanctions Program constitutes one of the most sophisticated economic sanctions programs ever devised and implemented. Because each component of the sanctions program is a targeted and justified response to a specific form of Russian aggression, many of our partners around the world—including European states as well as Canada, Australia, and Japan—have joined the United States in employing economic and financial restrictions.

The U.S. Russia Sanctions Program—which is now comprised of sectoral sanctions, list-based designations, secondary sanctions authority, and a comprehensive embargo—expanded most rapidly in 2014 following Russia's destabilizing activities in Ukraine—including the annexation of Crimea. Despite its sophistication, however, the Program is not comprehensive, and a number of avenues exist for a measured expansion. Assessing the benefits and drawbacks of those recommendations requires a baseline understanding of the current types of sanctions the United States has imposed on Russia, including the underlying rationale for their imposition. The current section provides an overview of U.S. sanctions already in place with respect to Russia's activities in Ukraine, cyber-enabled malicious activities, and human rights violations. It explains the reasoning behind each sanctions imposition—reasoning that informs when and how the United States should eventually unwind sanctions components based on changes in Russian behavior.

### *Destabilizing Activities in Ukraine*

In late February 2014, shortly after Ukraine's ex-president Viktor Yanukovich was forced out of Kiev by mass protests, Vladimir Putin gave an order for Russian Special Forces to begin "returning Crimea to Russia."<sup>9</sup> Gunmen planted the Russian flag at the local parliament in early March, setting the scene for a sham March 16 referendum in which Crimea purportedly voted to join the Russian Federation.<sup>10</sup>

Russian aggression continued following this de facto annexation of Crimea. Russian-backed separatists began seizing cities in eastern Ukraine; when Ukrainian forces appeared able to retake separatist-held territories, Russian reinforcements pushed the Ukrainians back.<sup>11</sup> An initial peace deal called the Minsk Protocol (or "Minsk I") failed, but in February 2015, the Minsk II ceasefire agreement ("Minsk II") was negotiated by the leaders of France, Germany, Ukraine, and Russia. Minsk II contains 13 points including, first, a commitment to the withdrawal of heavy weapons by both sides, monitored by the Organization for Security and Co-operation in Europe ("OSCE").

<sup>9</sup> Mary Ellen Connel and Ryan Evans, "Russia's 'Ambiguous Warfare' and Implications for the U.S. Marine Corps," *Center for Naval Analysis*, May 2015, [https://www.cna.org/CNA\\_files/PDF/TOP-2015-U-010447-Final.pdf](https://www.cna.org/CNA_files/PDF/TOP-2015-U-010447-Final.pdf).

<sup>10</sup> Alissa de Carbonnel, "How the Separatists Delivered Crimea to Moscow," *Reuters*, Mar. 13, 2014, <http://in.reuters.com/article/ukraine-crisis-russia-aksyonov-idINL6N0M93AH20140313>.

<sup>11</sup> "What Are The Minsk Agreements?" *The Economist*, Sept. 14, 2016, <http://www.economist.com/blogs/economist-explains/2016/09/economist-explains-7>.

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Minsk II also calls for the restoration of Ukraine's full control over its borders and for constitutional reform in Ukraine, among other points.<sup>12</sup>

In response to Russian aggression, the United States has employed three general categories of sanctions. First, the United States has imposed blocking sanctions on designated individuals and entities, adding them to the Treasury Department's Specially Designated Nationals List ("SDN List"), thereby freezing their assets and prohibiting transactions with U.S. persons. The blocking sanctions have been imposed on those undermining democratic processes and institutions in Ukraine; threatening the peace, security, stability, sovereignty, and territorial integrity of Ukraine; and contributing to the misappropriation of Ukraine's assets. Shortly after their initial imposition, these sanctions were extended to cover Russian government officials and persons operating in the Russian arms or related material sector.

Second, the United States has developed "sectoral sanctions" targeting selected entities in the financial, energy, and arms sectors of the Russian economy. These entities are listed on the Sectoral Sanctions Identification List ("SSI List"). Such sectoral sanctions generally prohibit U.S. persons from engaging in certain kinds of medium- and long-term transactions but generally allow day-to-day business activity; they also prohibit U.S. person involvement in many activities related to deep-water, Arctic offshore, or shale oil projects.

Third, the United States has imposed an investment ban and prohibition on the exportation or importation of goods, technology, or services to or from the Crimea region. These prohibitions constitute, in effect, a comprehensive embargo on Crimea.

The following authorities related to sanctions on Russia in response to its invasion of Ukraine are codified in the Ukraine Related Sanctions Regulations (31 C.F.R. Part 589).

<sup>12</sup> The core 13 components of the Minsk II Agreement include:

1. Immediate, full bilateral ceasefire as of 15 February 2015 at 00:00;
2. Withdrawal of all heavy weapons by both sides, to be completed within 14 days;
3. Effective monitoring regime for the ceasefire and withdrawal of heavy weapons by the OSCE;
4. Launch of dialogue on modalities of local elections in accordance with Ukrainian legislation;
5. Pardon and amnesty of figures involved in the conflict;
6. Release of all hostages and other illegally detained people, based on the "all for all" principle;
7. Safe delivery of humanitarian aid to those in need, based on an international mechanism;
8. Restoration of full social and economic links with affected areas;
9. Full Ukrainian control over its border with Russia throughout the conflict zone;
10. Withdrawal of all foreign armed groups, weapons and mercenaries from Ukrainian territory;
11. Constitutional reform in Ukraine with decentralisation as a key element; a new constitution by the end of 2015;
12. Local elections in Donetsk and Luhansk regions to be held according to OSCE standards; and
13. Intensifying of the work of the Trilateral Contact Group.

See Naja Bentzen, "Ukraine and the Minsk II Agreement: In a Frozen Path to Peace?" *European Parliamentary Research Service*, PE 573.951, Jan. 2016,  
[http://www.europarl.europa.eu/RegData/etudes/BRIE/2016/573951/EPRS\\_BRI\(2016\)573951\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2016/573951/EPRS_BRI(2016)573951_EN.pdf).

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- **Executive Orders 13660<sup>13</sup> and 13661<sup>14</sup>** (Mar. 6 and 16, 2014; 99 and 107 designations, respectively). By authorizing additions to the SDN List, these Orders block the property and interests in property of individuals and entities who have been determined to be responsible for, or complicit in actions or policies that undermine democratic processes or institutions in Ukraine or that threaten the peace, security, stability, sovereignty, or territorial integrity of Ukraine. In general, these designations include former Ukrainian public officials working with the Government of Russia, as well as individuals close to Russian President Vladimir Putin and other senior Russian government officials involved in planning activities in Ukraine.
- **Executive Order 13662<sup>15</sup>** (Mar. 20, 2014; 258 entities listed). This Executive Order authorizes the use of U.S. sectoral sanctions, which impose transaction-specific prohibitions on designated entities. U.S. sectoral sanctions are divided into four Directives, which target the Russian financial, defense, and energy sectors.
  - **Directive 1** (financial sector) prohibits U.S. persons from transacting in new debt of longer than 30 days maturity or new equity of designated financial institutions.
  - **Directive 2** (energy sector) prohibits U.S. persons from transacting in new debt of longer than 90 days maturity of designated energy companies.
  - **Directive 3** (defense sector) prohibits U.S. from transacting in new debt of longer than 30 days maturity of designated defense companies.
  - **Directive 4** (energy/unconventional oil) prohibits U.S. persons from providing goods, services (except for financial services), or technology in support of exploration or production for deep-water, Arctic offshore, or shale projects that have the potential to produce oil in Russia.
- **Executive Order 13685<sup>16</sup>** (Dec. 19, 2014; 47 designations). This Executive Order establishes a comprehensive embargo on the territory of Crimea, and U.S. persons are prohibited from investing in Crimea, and importing goods from—or exporting goods to—the area.
- **Ukraine Freedom Support Act<sup>17</sup>** (Dec. 18, 2014). Congress passed this Act to assist Ukraine in restoring its sovereignty and territorial integrity and to deter Russia from further destabilizing activities. While the Act did not result in new sanctions designations, it does establish new secondary sanctions authority. It provides the President with the authority

<sup>13</sup> Exec. Order No. 13,660, 79 Fed. Reg. 13,493 (Mar. 10, 2014), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo.pdf).

<sup>14</sup> Exec. Order No. 13,661, 79 Fed. Reg. 15,535 (Mar. 19, 2014), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo2.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo2.pdf).

<sup>15</sup> Exec. Order No. 13,662, 79 Fed. Reg. 16,167 (Mar. 24, 2014), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo3.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo3.pdf).

<sup>16</sup> Exec. Order No. 13685, 79 Fed. Reg. 247 (Dec. 19, 2014), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine\\_eo4.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo4.pdf).

<sup>17</sup> Ukraine Freedom Support Act of 2014, Pub. L. No. 113-272, 128 Stat. 2952 (2014), <https://www.congress.gov/113/plaws/publ272/PLAW-113publ272.pdf>.

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to impose sanctions on foreign companies that make significant investments in “special Russian crude oil projects,” which include Russia’s deep-water, Arctic offshore and shale projects. The Act also allows the President to prohibit or restrict the dealings of foreign financial institutions with the U.S. banking system if he determines that they have knowingly engaged in significant transactions involving sanctionable activities or sanctioned entities. To date the President has not designated entities under this authority.

*Malicious Cyber-Enabled Activities*

In late December, the United States acted in response to the Russian government’s cyber operations aimed at the United States. According to multiple U.S. intelligence agencies, Russia’s cyber activities were intended to sow doubt about the integrity of our electoral process and erode faith in liberal democracy.<sup>18</sup>

A pre-existing version of Executive Order 13694 of April 2015 had created a targeted authority for the U.S. Government to address cyber-enabled malicious activities that: (i) harm or significantly compromise the provision of services by entities in a critical infrastructure sector; (ii) significantly disrupt the availability of a computer or network of computers; or (iii) cause a significant misappropriation of funds or economic resources, trade secrets, personal identifiers, or financial information for commercial or competitive advantage or private financial gain.

Yet Russia’s use of cyber-enabled means to undermine democratic processes at home and abroad made clear that a tool explicitly targeting attempts to interfere with elections was also warranted.<sup>19</sup> The Executive Order was thus amended to authorize sanctions on those who tamper with, alter, or cause a misappropriation of information with the purpose or effect of interfering with or undermining election processes or institutions.

Using this new authority, the United States added nine entities and individuals to the SDN List: two Russian intelligence services (the GRU and the FSB); four officers of the GRU; and three companies that provided material support to the GRU’s cyber operations. The Treasury Department also designated two additional Russian individuals under the pre-existing Executive Order: one is responsible for the theft of over \$100 million from U.S. firms, universities, and agencies; the other compromised the computer networks of major U.S.-based e-commerce companies and misappropriated personal identifiers for financial gain.<sup>20</sup>

<sup>18</sup> “Background to ‘Assessing Russian Activities and Intentions in Recent US Elections’: The Analytic Process and Cyber Incident Attribution,” *Director of National Intelligence, Intelligence Community Assessment*, Jan. 6, 2017, [https://www.dni.gov/files/documents/ICA\\_2017\\_01.pdf](https://www.dni.gov/files/documents/ICA_2017_01.pdf).

<sup>19</sup> “FACT SHEET: Actions in Response to Russian Malicious Cyber Activity and Harassment,” *The White House*, Dec. 29, 2016, <https://obamawhitehouse.archives.gov/the-press-office/2016/12/29/fact-sheet-actions-response-russian-malicious-cyber-activity-and>.

<sup>20</sup> *Id.*

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- **Executive Order 13694**<sup>21</sup> (amended by E.O. 13757 of Dec. 28, 2016;<sup>22</sup> 11 designations). E.O. 13694 authorized the imposition of sanctions on individuals and entities determined to be responsible for malicious cyber-enabled activities that constitute a significant threat to the national security, foreign policy, or economic health or financial stability of the United States.

#### *Human Rights Violations*

Following the death of Sergei Magnitsky, a political activist who suspiciously died in prison on November 16, 2009 after uncovering fraud involving Russian tax officials,<sup>23</sup> Congress passed the Magnitsky Act. This act aimed to punish Russian officials involved in his death and in the corruption he uncovered as well as individuals determined to be responsible for gross violations of human rights. Most recently, on January 9, 2017, the United States designated five additional Russians, “including powerful senior law-enforcement official Aleksandr Bastrykin and lawmaker Andrei Lugovoi, who has been accused in Britain in the poisoning of Kremlin critic Aleksandr Litvinenko.”<sup>24</sup>

- **Sergei Magnitsky Rule of Law Accountability Act of 2012**<sup>25</sup> (Dec. 14, 2012; 44 designations). This legislation requires that sanctions be imposed on individuals determined, based on credible information, to be responsible for the detention, abuse, or death of Sergei Magnitsky; who have participated in efforts to conceal the legal liability for, or who have financially benefited from the detention, abuse, or death of Magnitsky; or were involved in the criminal conspiracy uncovered by Magnitsky.<sup>26</sup> This legislation also requires that sanctions be imposed on individuals determined to be responsible for extrajudicial killings, torture, or other gross violations of internationally recognized human rights committed against individuals seeking to expose illegal activity carried out by officials of the Russian Government, or seeking to obtain, exercise, defend, or promote internationally recognized human rights and freedoms in Russia.<sup>27</sup>

## **II. Gauging the Effectiveness of U.S. Sanctions on Russia**

<sup>21</sup> Exec. Order No. 13694, 80 Fed. Reg. 18,077 (Apr. 2, 2015), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/cyber\\_eo.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/cyber_eo.pdf).

<sup>22</sup> Exec. Order No. 13757, 82 Fed. Reg. 1 (Jan. 3, 2017), available at [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/cyber2\\_eo.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/cyber2_eo.pdf).

<sup>23</sup> “Announcement of Sanctions Under the Sergei Magnitsky Rule of Law Accountability Act,” *Treasury Department Press Center*, May 20, 2014, <https://www.treasury.gov/press-center/press-releases/Pages/j12408.aspx>.

<sup>24</sup> Carl Shreck, “U.S. Sanctions Russia’s Bastrykin and Alleged Litvinenko Killers,” *Radio Free Europe Radio Liberty*, Jan. 10, 2017, <http://www.rferl.org/a/russia-bastrykin-lugovoi-magnitsky-sanctions/28222295.html>.

<sup>25</sup> Russia and Moldova Jackson-Vanik Repeal and Sergei Magnitsky Rule of Law Accountability Act of 2012, Pub. L. No. 112-208, Dec. 2014, <https://www.congress.gov/112/plaws/publ208/PLAW-112publ208.pdf>.

<sup>26</sup> “Announcement of Sanctions Under the Sergei Magnitsky Rule of Law Accountability Act,” *Treasury Department Press Center*, May 20, 2014, <https://www.treasury.gov/press-center/press-releases/Pages/j12408.aspx>.

<sup>27</sup> *Id.*



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The effectiveness of these various sanctions programs is mixed; economic and political indicators suggest that they have had an impact on the Russian economy and Russian decision-making, though not sufficient to coerce Russia to cease its aggressive cyber activity, relinquish control over Crimea, or cease its support for separatists in Eastern Ukraine.<sup>28</sup>

#### *Imposing Economic Costs*

The Russian economy has clearly struggled since the broadest sanctions were imposed in 2014,<sup>29</sup> but the downturn was likely driven both by the collapse in global oil prices and the imposition of sectoral sanctions. For example, the Congressional Research Service notes that most sanctions hit just as the oil price was dropping by more than 60% between the start of 2014 and the end of 2015.<sup>30</sup> Yet the sanctions do appear to have had an independent impact at the macroeconomic level; a 2015 IMF estimate that “U.S. and EU sanctions in response to the conflict in Ukraine and Russia’s countervailing ban on agricultural imports reduced Russian output over the short term by as much as 1.5%.”<sup>31</sup> In April 2015, speaking to the lower house of parliament in Moscow about “unprecedentedly harsh sanctions pressure,” Russian Prime Minister Dmitry Medvedev said that the sanctions had cost Russia \$26.7 billion in 2014 and would cost \$80 billion more in 2015.<sup>32</sup>

The sanctions may have exerted their greatest impact through changes in foreign investment and at the firm level. As the work of one of my fellow witnesses showcases, the sanctions created an atmosphere that discouraged foreign direct investment and that this “lower investment in Russia could lead to a cumulative loss of output of up to 9 percent of GDP.”<sup>33</sup> Likewise, her work also found that U.S. targeted sanctions, while not specific to the Russia program, cause countries to “face significantly elevated levels of political risk, depressing investment in the target’s economy.”<sup>34</sup> Data compiled by the Congressional Research Service corroborates this finding.

<sup>28</sup> The question of whether these sanctions have been effective touches on a wide range of other issues not addressed here, such as whether the employment of these tools in the current situation will deter future aggression by Moscow or by other states whose leaders are observing Russia’s tactics with great interest. This testimony focuses directly on the economic impact of these tools and whether and how they have changed Russian decision making in the short term, related to the issues of Ukraine, cyber activities, and human rights abuses.

<sup>29</sup> Note that it is difficult to differentiate between the economic impacts of the various sanctions programs described above. Most of the studies focused on the economic impact of these sanctions pay particular attention to the Ukraine-related sanctions, and in particular the SSI program, as these are the broadest coercive measures the United States and the EU have employed against Russia. In reality, these sanctions programs have interactive effects, to an extent; for example, additional designations related to Russia’s malicious cyber-enabled activities likely signal to foreign investors that tensions will continue between the United States and Russia, likely depressing FDI.

<sup>30</sup> Rebecca Nelson, “U.S. Sanctions and Russia’s Economy,” *Congressional Research Service*, Feb. 17, 2017,

<https://fas.org/sgp/crs/row/R43895.pdf>.

<sup>31</sup> *Id.* At 6-7.

<sup>32</sup> Ed Adamczyk, “Medvedev: Sanctions Cost Russia \$106 Billion,” *UPI*, Apr. 22, 2015, [http://www.upi.com/Top\\_News/World-News/2015/04/22/Medvedev-Sanctions-cost-Russia-106-billion/3551429721857/](http://www.upi.com/Top_News/World-News/2015/04/22/Medvedev-Sanctions-cost-Russia-106-billion/3551429721857/).

<sup>33</sup> Elizabeth Rosenberg, Daniel Drezner, Julia Solomon-Strauss, and Zachary Goldman, “The New Tools of Economic Warfare: Effects and Effectiveness of Contemporary U.S. Financial Sanctions,” *Center for a New American Security*, Apr. 2016, <https://www.cnas.org/publications/reports/the-new-tools-of-economic-warfare-effects-and-effectiveness-of-contemporary-u-s-financial-sanctions>.

<sup>34</sup> *Id.* at 1.

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showing that net inward FDI into Russia “essentially came to a halt in late 2014 and early 2015,” consistent with the general finding.<sup>35</sup> As a former economic advisor to the Russian government stated in 2015, the sectoral sanctions in particular had “worked out as far more severe in their effect than anyone seems to have believed.”<sup>36</sup>

Likewise, research conducted by another witness on this panel suggests that targeted firms are also feeling this impact, finding that “the average sanctioned company or associated company loses about one-third of its operating revenue, over one-half of its asset value, and about one-third of its employees relative to their non-sanctioned peers.”<sup>37</sup> That U.S. sanctions are “hitting their intended targets” without causing too much “collateral damage,” as the paper concludes, is important, as it suggests that designations can be carefully ramped up to respond to further Russian provocations. As former Deputy National Security Advisor Juan Zarate and Russia expert at the Center on Sanctions and Illicit Finance at the Foundation for Defense of Democracies Boris Zilberman argue, “Russia’s corporations, particularly the titans of industry, are heavily linked to Putin and his inner circle. As such, the Kremlin is often forced to bail out companies via corporate debt assistance as they deal with fallout from sanctions and low oil prices. By maintaining and potentially increasing economic pressure on these companies, the U.S. and E.U. can force the Kremlin to spend more of its money, more often, to prop up a growing list of state-dependent corporations.”<sup>38</sup>

Despite the macroeconomic and firm-level impact of the U.S. sanctions on Russia, both the IMF and the Bank of Russia’s research and forecasting department project positive Russian GDP growth in 2017.<sup>39</sup> This does not necessarily mean that sanctions have ceased to cause macroeconomic pain: a survey of experts suggests that the Russian economy would receive an additional lift—of 0.2% this year and 0.5% in 2018—if U.S. sanctions were relaxed.<sup>40</sup> Still, Russia has weathered the sanctions program and the concurrent oil price collapse, and improvements in its economy do suggest that U.S. restrictions impose less cost now than they have in the past. The bottom line is that these sanctions have had an impact on the Russian economy, though that impact appears to be diminishing.

<sup>35</sup> Rebecca Nelson, “U.S. Sanctions and Russia’s Economy,” *Congressional Research Service*, Feb. 17, 2017, <https://fas.org/spp/crs/row/R43895.pdf>.

<sup>36</sup> Priyanka Boghani, “What’s Been the Effect of Western Sanctions on Russia?” *PBS Frontline*, Jan. 13, 2015, <http://www.pbs.org/wgbh/frontline/article/whats-been-the-effect-of-western-sanctions-on-russia/>.

<sup>37</sup> Daniel Ahn and Rodney Ludema, “Measuring Smartness: Understanding the Economic Impact of Targeted Sanctions,” Working Paper 2017-01, *U.S. Department of State, Office of the Chief Economist*, Dec. 2016, <https://www.state.gov/documents/organization/267590.pdf>.

<sup>38</sup> Juan Zarate and Boris Zilberman, “U.S. Russian Financial Warfare: Conduct-Based Approach to Countering Russian Influence and Increasing Western Leverage,” Working Paper, *Center on Sanctions and Illicit Finance, Foundation for Defense of Democracies*, on file with author.

<sup>39</sup> “IMF Staff Concludes Visit to Russian Federation,” *International Monetary Fund Press Release*, No. 16/529, Nov. 29, 2016, <http://www.imf.org/en/News/Articles/2016/11/29/PR16529-Russian-Federation-IMF-Staff-Concludes-Visit>. See also Anna Andrianova, “Russia is Running on More Than Just the Black Stuff,” *Bloomberg*, Mar. 7, 2017, <https://www.bloomberg.com/news/articles/2017-03-07/russia-is-running-on-more-than-just-the-black-stuff>.

<sup>40</sup> Anna Andrianova, “Russia is Running on More Than Just the Black Stuff,” *Bloomberg*, Mar. 7, 2017, <https://www.bloomberg.com/news/articles/2017-03-07/russia-is-running-on-more-than-just-the-black-stuff>.

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*Coercing Change in Behavior*

It is harder to point to tangible indications that sanctions have altered Russian behavior with respect to Ukraine, malicious cyber-enabled activities, or human rights violations. Journalists, rights advocates, opposition politicians, and whistleblowers are still treated harshly and sometimes killed.<sup>41</sup> On the cyber front, Ukraine last month “accused Russian hackers of targeting its power grid, financial system and other infrastructure with a new type of virus that attacks industrial processes.”<sup>42</sup> Montenegro claimed in mid-February that government and media websites came under Russian attack for several days.<sup>43</sup> A French presidential candidate claims that he is being targeted with “[I]nternet attacks from within Russia with the goal of helping the campaigns of his pro-Moscow rivals.”<sup>44</sup> In short, Russia’s malicious cyber efforts are continuing.

Russia shows no sign of relinquishing control of Crimea, and it continues to destabilize eastern Ukraine. Just last week, Kiev threatened sanctions against the Ukrainian subsidiary of Kremlin-owned Sberbank because the bank said it would comply with an order from Vladimir Putin to recognize identity documents issued in the separatist-held regions of Donetsk and Luhansk.<sup>45</sup> Fighting recently flared up in places like Sartana, a farming village near the Ukrainian-held port of Mariupol, after months of relative quiet: on the Ukrainian side alone, at least 26 people were killed and 124 wounded in the month after January 28 compared to eight dead and 46 wounded in the month prior.<sup>46</sup> A new ceasefire to address the flare-up seems to have failed.<sup>47</sup> On February 26, the State Department, recognizing Russia’s unwillingness to meet its obligations under Minsk II, called on “Russia and the separatist forces it backs” to “honor the cease-fire called for under the Minsk agreements” and to “withdraw all heavy weapons, and allow full and unfettered access to the OSCE monitors.”<sup>48</sup>

Nevertheless, some organizations and analysts believe that sanctions have had some impact on behavior because, in their absence, Russia would likely have gone further in Ukraine. Former

<sup>41</sup> Andrew Kramer, “More of Kremlin’s Opponents Are Ending Up Dead,” *The New York Times*, Aug. 20, 2016, <https://www.nytimes.com/2016/08/21/world/europe/moscow-kremlin-silence-critics-poison.html>.

<sup>42</sup> Natalia Zinets, “Ukraine Charges Russia with New Cyber Attacks on Infrastructure,” *Reuters*, Feb. 15, 2017, <http://www.reuters.com/article/us-ukraine-crisis-cyber-idUSKBN1SU2CN>.

<sup>43</sup> Ben Farmer, “Montenegro Asks for British Help after Cyber Attacks in Wake of ‘Russian-backed coup plot,’” *The Telegraph*, Feb. 28, 2017, <http://www.telegraph.co.uk/news/2017/02/28/montenegro-asks-british-help-cyber-attacks-wake-russian-backed/>.

<sup>44</sup> “France Drops Electronic Voting for Citizens Abroad over Cybersecurity Fears,” *Reuters*, Mar. 6, 2017, <http://www.reuters.com/article/us-france-election-cyber-idUSKBN16D233?l=0>.

<sup>45</sup> “Ukraine Eyes Sanctions on Subsidiary of Russia’s Sberbank,” *Reuters*, Mar. 7, 2017, <http://www.reuters.com/article/us-ukraine-crisis-sanctions-idUSKBN16E2KL>.

<sup>46</sup> Mark Mackinnon, “As Russia-U.S. Ties Strengthen, Violence Escalates in Ukraine,” *The Globe and Mail*, Feb. 26, 2017, <http://www.theglobeandmail.com/news/world/as-russia-us-ties-strengthen-violence-escalates-inukraine/article34143679/>.

<sup>47</sup> Euan McKirdy, “Ukraine Ceasefire: No Sign of Withdrawal, Official Says,” *CNN*, Feb. 23, 2017, <http://www.cnn.com/2017/02/22/europe/ukraine-ceasefire-violations/>.

<sup>48</sup> Mark C. Toner, “United States Condemns Attack on Special Monitoring Missions in Eastern Ukraine,” Press Statement, *United States Department of State*, Feb. 26, 2017, <https://www.state.gov/r/pa/prs/ps/2017/02/268039.htm>.

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Deputy Assistant Secretary of State Peter Harrell observed in September 2015 that “Russia does appear to have made tactical adjustments to its strategy at different points during the crisis to minimize the odds of [further] sanctions being imposed.”<sup>49</sup> In his view, the demonstrated effect of sanctions and the threat of broader measures “may have helped deter Russia from moving forward and seizing the strategic city of Mariupol” in February 2015.<sup>50</sup> A March 2016 publication of the European Parliament argued that sanctions were deterring further violence, again pointing to the Black Sea port of Mariupol.<sup>51</sup>

In addition, at least in the context of Ukraine, Vladimir Putin and Foreign Minister Sergei Lavrov have explicitly called for<sup>52</sup> and even demanded<sup>53</sup> an end to sanctions. Russia has also worked to undermine EU unity on sanctions, including by “methodically lobbying southern and eastern EU member states,” with Italy, Greece, Hungary, Cyprus, Slovenia, Slovakia and Bulgaria as prime targets.<sup>54</sup> Some analysts believe that Moscow may be aiding populist parties—including in Western European countries—because it sees these parties as “useful allies in pursuing its objectives in Europe, such as ending economic sanctions or undermining European support for Ukraine.”<sup>55</sup> These demands and efforts suggest that, even if the sanctions have not fulfilled all of the objectives they were initially employed to achieve, they do appear to be impacting Russian decision making. In addition, these comments suggest that the sanctions provide the United States with leverage it would not otherwise have; clearly the Russian leadership would like to have the sanctions lifted, and this desire means that the United States can exchange relief for certain concessions from Moscow. To unwind them without consideration of this fact and without seeing change in Russian behavior would be a strategic mistake.

Thus, while our sanctions on Russia have not proven to be a silver bullet, there are indications that they have had an impact on the Russian economy and on Russian decision-making. Additional sanctions pressure would likely further impact Russia’s decision calculus, and, if done responsibly,

<sup>49</sup> Peter Harrell, “Lessons from Russia on the Future of Sanctions,” *Center for a New American Security*, Sept. 2015, <https://s3.amazonaws.com/files.cnas.org/documents/CNAS-Report-Economic-Statecraft-2-FINAL.pdf>.

<sup>50</sup> *Id.* at 6.

<sup>51</sup> Martin Russell, “Sanctions over Ukraine: Impact on Russia,” *European Parliamentary Research Service*, PE 579.084, Mar. 2016, <http://www.europarl.europa.eu/EPRS/EPRS-Briefing-579084-Sanctions-over-Ukraine-impact-Russia-FINAL.pdf>.

<sup>52</sup> “Russia Can’t Mend Times with U.S. While it Backs Sanctions: Lavrov,” *Reuters*, Dec. 10, 2015, <http://www.reuters.com/article/us-russia-usa-lavrov-idUSKBN0T0YR20151210>; David Herszenhorn, “Putin Calls for End to Use of Sanctions and Criticizes U.S. in Afghanistan,” *The New York Times*, July 10, 2015, <https://www.nytimes.com/2015/07/11/world/europe/putin-criticizes-us-role-in-afghanistan.html>; On statement regarding EU sanctions, see “EU Releases Details on Extended Sanctions Against Russia,” *Voice of America News*, June 18, 2016, <http://www.voanews.com/a/european-union-releases-details-extended-sanctions-russia/3382180.html>.

<sup>53</sup> Roland Oliphant, “‘Cancel Sanctions and Scale Back NATO’ Russia Tells US as Vladimir Putin Scraps Nuclear Deal,” *The Telegraph*, Oct. 3, 2016, <http://www.telegraph.co.uk/news/2016/10/03/putin-scraps-deal-to-dispose-of-bomb-grade-plutonium-in-swipe-at/>.

<sup>54</sup> “Putin Steps Up Drive to Kill Sanctions Amid Signs of EU Disunity,” *Voice of America News*, July 29, 2016, <http://www.voanews.com/a/putin-steps-up-drive-kill-sanctions-signs-eu-disunity/3440262.html>.

<sup>55</sup> Arthur Beesley, “EU Leaders to Hold Talks on Russian Political Meddling,” *Financial Times*, Oct. 16, 2016, <https://www.ft.com/content/ff1f1cdc-9227-11e6-8df8-d3778b55a923>.

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could help the United States pressure Moscow to change its behavior in Ukraine, cyber, and in the realm of human rights abuses.

### III. Increasing the Pressure on Russia, Responsibly

The United States and its partners can take a number of steps to increase pressure on Russia in a way that will squeeze its economy and—more importantly—impact its decision making. Recent legislative initiatives in the Senate, including the proposed Counteracting Russian Hostilities Act of 2017 (“Counteracting Russian Hostilities Act”)<sup>56</sup> and the proposed Russia Sanctions Review Act of 2017 (“Russia Sanctions Review Act”),<sup>57</sup> are right steps in this direction. In particular, the Counteracting Russian Hostilities Act would impose powerful sanctions on Russia, including primary and secondary sanctions related to its petroleum industry, the Russian defense sector, and the Russian financial sector.

However, as Congress considers ramping up sanctions on Russia, it should keep in mind that while such pressure is important, the United States should try—to the extent possible—to ensure that the sanctions are carefully targeted and do not have unintended and undesirable impacts. For example and as occurred during the initial Sectoral Sanctions Identifications List program ramp up in the fall and winter of 2014, the sanctions pressure on Russia deeply shook investor confidence and threatened the stability of the Russian financial system. Indeed, in December 2014, U.S. sanctions—in conjunction with other factors—led to a near run on the Ruble, which was supposedly triggered by the Central Bank of Russia promising to effectively print money to prop up certain companies owned by Putin’s confederates and hurt by Western sanctions.<sup>58</sup> While the U.S. sanctions on Russia were meant to impact the Russian economy in the medium- to- long-term and to put pressure on Vladimir Putin and his elite circle, they were not intended to cause a run on the currency, which could have seriously undermined the stability of the Russian financial sector.

While the United States certainly should pressure Moscow, undermining the stability of one of the world’s largest economies would have serious and detrimental ripple effects. In effect, Congress should carefully balance increasing the economic pressure on Russia while making sure that any steps it takes do not risk collapsing the Russian economy or seriously impacting the economic health of our partners, particularly in the European Union and Eastern Europe.

On this point, Congress must consider the impact ramping up sanctions will have on our European partners, and in particular whether they will be willing to join our efforts. Over the past three years, the United States and the European Union have worked very closely to ramp up pressure on Russia; while there are minor differences between the U.S. and the EU sanctions programs in

<sup>56</sup> S. 94, “Counteracting Russian Hostilities Act of 2017,” 115<sup>th</sup> Cong. (2017).

<sup>57</sup> S. 1, “Russia Sanctions Review Act of 2017,” 115<sup>th</sup> Cong. (2017).

<sup>58</sup> [http://bigassets.huffingtonpost.com/Russia\\_Sanctions\\_Review\\_Act.pdf](http://bigassets.huffingtonpost.com/Russia_Sanctions_Review_Act.pdf).

<sup>59</sup> Peter Feaver and Eric Lorber, “The Sanctions Myth,” *The National Review*, July-August 2015, <http://nationalinterest.org/feature/the-sanctions-myth-13110?page=2>. See also Sergey Aleksashenko, “Evaluating Western Sanctions on Russia,” *Atlantic Council*, Dec. 2016 at 10, [http://www.atlanticcouncil.org/images/publications/Evaluating\\_Western\\_Sanctions\\_on\\_Russia\\_web\\_1206.pdf](http://www.atlanticcouncil.org/images/publications/Evaluating_Western_Sanctions_on_Russia_web_1206.pdf).

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response to Russian aggression in Ukraine, in general these programs—and targeted entities—are the same. In fact, the EU SSI-type program is in some ways more restrictive than the U.S. SSI program. This close partnership has significantly increased the economic impact on Moscow; Russian entities were unable to turn to attractive alternative partners in the EU to secure financing, for example, when they were cut off from U.S. debt markets.

While certain countries such as Germany have signaled a willingness to ramp up pressure on Russia, other EU countries may be less willing to join U.S. efforts. To the extent that we can secure European buy-in—and parallel European escalation of economic pressure—our sanctions will stand a greater chance of success. Likewise, when considering certain sanctions proposals put forth below, Congress should be mindful of their impact on European cooperation. For example, those proposals that impose restrictions on the activities of both U.S. and non-U.S. companies will likely raise political tensions with the Europeans. To the extent that the United States can secure EU cooperation on many of these matters without resorting to U.S. domestic legislation that conditions access to U.S. markets on compliance with our sanctions policy, the more likely our approach will be to succeed.

Recent legislative proposals contain excellent steps for imposing powerful sanctions that will likely impact Russian decision-making. By further sharpening these tools, Congress can ensure that it raises the pressure on Russia in a way that both directly targets Moscow's decision makers and limits the impact on our allies and partners. The proposals outlined below are generally ordered from least likely to impose significant additional economic pain and create possible unintended consequences to most likely to impose such pain and create such consequences. In effect, each subsequent option is likely more powerful, yet also likely riskier, than the preceding option.<sup>59</sup> For those more-powerful-yet-riskier tools, I have suggested adjustments that may limit some of their potential downsides.

This **sanctions escalation ladder** should provide Congress with a range of options, depending on how much pressure it wants to put on Moscow.

- **Rung #1: Codification of existing Executive Orders**, including Executive Orders 13660, 13661, 13662, 13685, and 13694. At a minimum, Congress should act to preserve the sanctions currently in place on Russia. The reason for the creation of these executive authorities—and the designations issued pursuant to them—has not changed; Russia has not fulfilled its obligations under Minsk II, has not meaningfully reduced its aggressive cyber activity towards the United States, and as the recent episode with Vladimir Kara-

<sup>59</sup> Note that I do not review the proposals contained in the Russia Sanctions Review Act. While there is certainly room for congressional approval and disapproval of waiving certain components of the U.S. Russia Sanctions Program, the Russia Sanctions Review Act focuses on how to limit the administration from unwinding current sanctions on Russia, not on how to increase the pressure on Moscow. Given that sanctions on Russia have been somewhat effective and that additional economic pressure may likewise have an impact, I have focused on how to responsibly ramp up pressure rather than maintain the status quo.

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Murza suggests,<sup>60</sup> has not significantly improved its human rights record. Without improvements in these areas, Moscow should not be rewarded with the lifting of sanctions, and Congress should take steps to ensure that does not happen. Unwinding these programs and de-designating entities in exchange for Moscow's help in fighting certain extremist elements, either in Syria or elsewhere, risks seriously undermining the international principles that underpinned the U.S. and EU decisions to impose such measures. For example, if the United States unwinds its sanctions program on Russia as part of a "grand bargain" for Russian help fighting extremism—and Russia is allowed to maintain control of Crimea and continue supporting separatist movements in Eastern Ukraine—states that seek to violate the sovereignty of neighboring countries will know that the United States does not prioritize enforcement in response to territorial aggression. Such an unwinding also undermines the future effectiveness of U.S. sanctions. If sanctions targets can simply wait for a change in political circumstances, they will not be motivated to make the concessions that the United States demands. Instead, violators will take increased hope in the possibility that they can outlast economic restrictions because the United States will inevitably shift its foreign policy priorities.

In addition to simply codifying these Executive Orders, Congress could statutorily designate a range of other targets pursuant to these authorities. For example, Congress could designate additional individuals known to engage in cyber operations against the United States, military or administrative officials playing an active role in Eastern Ukraine or Crimea, or other high-level officials within the Russian government. Such additional pressure—particularly coupled with an increased focus by the proposed FinCEN-led task force discussed below—could significantly impact Putin's inner circle, bottom line, and decision-making.<sup>61</sup> In addition, Congress could specify that these designations only be lifted in the case of tangible and measurable progress by Russia on a range of issues, such as fulfillment of certain obligations under Minsk II.

- **Rung #2: Establishing a task force dedicated** to identifying, tracking, tracing and—as appropriate—**seizing assets of designated Russian individuals**, particularly those close to Russian President Vladimir Putin. The Countering Russian Hostilities Act recommends the creation of a Russia task force within the Financial Crimes Enforcement Network at the Treasury Department, which will work with the Office of Foreign Assets Control ("OFAC") and the Office of Intelligence and Analysis ("OIA") to identify certain illicit Russian assets within the United States. A creation of this type of standing entity could be particularly powerful; based on information gathered in recent years from title insurers under the FinCEN Geographic Targeting Order targeting certain high-end real estate markets, it is clear that large sums of Russian money are flowing into U.S. real estate

<sup>60</sup> Andrew Kramer, "More of Kremlin's Opponents Are Ending Up Dead," *The New York Times*, Aug. 20, 2016, <https://www.nytimes.com/2016/08/21/world/europe/moscow-kremlin-silence-critics-poison.html>.

<sup>61</sup> S. 94, "Countering Russian Hostilities Act of 2017," 115<sup>th</sup> Cong. (2017) at 47-48.

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markets.<sup>62</sup> It is very likely that designated Russian persons—including Russian oligarchs close to Russian President Vladimir Putin—are laundering their funds through a network of shell companies and depositing them within the United States. Seizing the assets of these designated persons would have an immediate impact on their pocketbooks and could put direct pressure on Putin's inner circle.

To be effective, such a task force would need to focus more broadly than high-end real estate, and would need to conduct deep dives into company formation information and beneficial ownership information of key bank accounts. In addition, it would need to be properly resourced; effectively establishing such a task force would require proper staffing, including the creation of dedicated positions (without simply shifting personnel from other important roles within Treasury). In addition, while FinCEN in some ways is a natural fit for this task force, given its access to information provided by U.S. financial institutions, Congress should consider including other, relevant agencies, such as the Department of Justice.

Congress should also consider requiring regular reporting from this task force on its findings and, based on that information, statutory PATRIOT Act 311 designations of Russian financial institutions engaged in illicit activity. Such designations would further squeeze the Russian financial sector and cut off illicit financial actors from the legitimate global banking system, though such efforts may take years to reach fruition.

- **Rung #3: Prohibiting the purchase, subscription to, or facilitation of the issuance of Russian sovereign debt.** This suggestion—contained in the Counteracting Russian Hostilities Act—is meant to address a gap in the current SSI program; that Russia may be using capital injections to prop up government-owned entities, as well as designated private companies owned or controlled by Vladimir Putin's allies in Russia. In effect, though financial institutions designated as SSIs pursuant to Directive 1 may not be able to secure debt financing, Russia itself can, and then can provide direct funds to those entities in a scheme that looks very much like sanctions evasion. By prohibiting U.S. and foreign persons from purchasing or generally dealing in such debt, this suggestion could cut off this sanctions evasion mechanism and make it significantly more difficult for Russia to prop up a number of its core financial institutions.

According to the IMF, Russia's international reserves dropped from \$509.6 billion at the beginning of 2014 to \$368.4 billion at the end of 2015, but they have increased slightly and remained stable at just below \$400 billion since the decline.<sup>63</sup> That decline during 2014-15 coincided with the sharpest oil price drop, during which time Russia was forced to sell foreign exchange to support the ruble.

<sup>62</sup> Josh Barbanel, Samuel Rubinfeld, and Laura Kusisto, "U.S. Expands Real-Estate Data Targeting Order," *The Wall Street Journal*, July 27, 2016, <https://www.wsj.com/articles/u-s-expands-real-estate-data-targeting-order-1469647229>. Note that this Order was again extended in February 2017.

<sup>63</sup> "Russian Federation, Staff Report for the 2016 Article IV Consultation," *International Monetary Fund*, IMF Country Report No. 16/229, July 2016, <http://www.imf.org/external/pubs/ft/scr/2016/cr16229.pdf>.



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Russia has drained one of its sovereign wealth funds, the Reserve Fund, from \$87 billion in 2014 to roughly \$16 billion currently; its other sovereign wealth fund, the National Wealth Fund—designed to support pensions and social spending—contains \$73 billion, but most of that amount has already been allocated.<sup>64</sup> Still, as noted above, international reserves have remained stable. According to Bloomberg, “by printing rubles for the Finance Ministry and crediting foreign currency to its own account, the central bank has kept international reserves—which include the government’s savings—almost intact even as the [Reserve Fund] has dwindled.”<sup>65</sup> Analysts expect that the Reserve Fund will be drained in 2017, but it is unclear what significance this will have.<sup>66</sup>

One of the major unknowns of this proposal is the magnitude of the economic impact it would have on Russia. While it would no doubt impact SSI designated-entities’ ability to balance their sheets and remain solvent, concerns exist that it would significantly destabilize the Russian financial system and create a significant contagion effect. To mitigate such concerns, Congress could structure such a prohibition to apply only to U.S. persons or where a U.S. nexus is involved. Such a structure would permit foreign financial institutions to transact in this foreign debt without fear of secondary sanctions. However, given the expansive reach of U.S. jurisdiction over the international financial system and U.S. regulators’ willingness to impose significant fines on entities violating U.S. sanctions regulations, most large and reputable financial institutions would be understandably extremely reluctant to transact in such sovereign debt. This reluctance would translate into market impact; the decrease in buyers of the debt would mean that Russia would have to offer higher interest rates to find market partners, ensuring that Moscow would have to pay more to borrow. Such a move would increase the costs on Russia but would also be unlikely to seriously undermine the Russian financial sector.

In addition, Congress could include a provision of the legislation that allows for the imposition of penalties to all persons (not simply U.S. persons) who transact in Russia sovereign debt in the case of continued Russian non-compliance on a range of items, such as fulfilling its Minsk II obligations. For example, Congress could build in a six-month assessment review of the impact of these sanctions and—if it was not satisfied that such a prohibition for U.S. persons on dealing in Russian sovereign debt was having a sufficient impact—could automatically expand the provision to apply to all persons. Such an expansion could be a powerful escalation, but undertaken only after verification that the initial sanction was not having the desired impact.

<sup>64</sup> Josh Meakins, “Why Russia is Far Less Threatening Than It Seems,” *Washington Post Monkey Cage*, Mar. 8, 2017, [https://www.washingtonpost.com/news/monkey-cage/wp/2017/03/08/why-russia-is-far-less-threatening-than-it-seems/?utm\\_term=.901bc86a6fa1](https://www.washingtonpost.com/news/monkey-cage/wp/2017/03/08/why-russia-is-far-less-threatening-than-it-seems/?utm_term=.901bc86a6fa1)

<sup>65</sup> Olga Tanas, Ilya Arkhipov, and Evgenia Pismennaya, “Russia Said to Shield Reserves as Putin Taps Sovereign Fund,” *Bloomberg*, June 28, 2016, <https://www.bloomberg.com/news/articles/2016-06-28/bank-of-russia-said-to-shield-reserves-as-putin-taps-wealth-fund>

<sup>66</sup> Nadia Kazakova, “Russian Ruse Keeps Currency Reserves Afloat,” *Saxo Group*, July 8, 2016, <https://www.tradingfloor.com/posts/russian-ruse-keeps-currency-reserves-afloat-7897510>

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- **Rung #4: Increasing the pressure on the Russian oil, gas, and petrochemical industries.** Another pathway to significantly pressure Russia would be to more expansively target its oil, gas and petrochemical industries. While Directives 2 and 4 of the SSI program target the health of Russia's petroleum industry in the medium-to-long terms (by targeting the development of resources that would come online during that time frame), they have not put as much pressure on Russia's economic resources in the shorter term. Similarly, proposals contained in the Counteracting Russian Hostilities Act also focus on the medium term; by penalizing U.S. and foreign persons that broadly invest in Russian energy resources, the United States would certainly impact the ability of the Russian Federation to produce such resources in a cost-effective way. Yet with the rising price of oil, such measures might not have an immediate or powerful impact in the short term, and consequently may not change Russia's activity during that time frame.

In addition to the recommendations proposed in the Counteracting Russian Hostilities Act, particularly Section 207(a), Congress should consider additional sanctions that pressure Russian energy companies in the short term.

First, Congress should consider imposing export restrictions on crude oil produced by three Russian major companies, namely Gazpromneft, Bashneft, and Rosneft. According to one study, these three companies account for almost 50% of Russian crude oil exports.<sup>67</sup> While these targets could still sell oil elsewhere, it would cost more to do so and impose limited punishment on the Russian Government.

To be effective, such sanctions would need to be constructed as secondary in nature, *i.e.*, threatening to cut European and Asian companies off from U.S. markets if their home countries continue to import certain hydrocarbon products from these companies. Such a step would likely cause significant diplomatic tension, particularly with our partners in the European Union. To mitigate such tension, the statutory provision could be structured to give the administration six months to work with the Europeans to draw down their reliance on petroleum products produced by these entities. If, at the end of that period, an insufficient drawdown had occurred, Congress could reserve the prerogative to impose secondary sanctions on targeted companies in the EU and Asia. Congress could also write in a significant reduction or national security exception element to this provision, much like the provision included in the National Defense Authorization Act Sec. 1245 in the Iran context, to ensure that we would not unduly be punishing our allies or seriously undermining the economies of our partners, particularly those in Eastern Europe who are highly reliant on Russian energy exports. Such a provision could either be in lieu of, or in addition to, the six-month period to allow the administration to convince countries in Europe and Asia to draw down.

<sup>67</sup> Sergey Aleksashenko, "Evaluating Western Sanctions on Russia," *Atlantic Council*, Dec. 2016, [http://www.atlanticcouncil.org/images/publications/Evaluating\\_Western\\_Sanctions\\_on\\_Russia\\_web\\_1206.pdf](http://www.atlanticcouncil.org/images/publications/Evaluating_Western_Sanctions_on_Russia_web_1206.pdf).

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Second, Congress could consider prohibiting correspondent accounts and payable access for financial institutions providing banking services on behalf of key Russian oil-producing companies. Such a move would have an immediate and powerful impact on these companies, as the global oil trade is primarily dollar-based. In effect, if these companies were unable to do oil transactions in dollars, they would need to use alternative currencies, a time-consuming and expensive process. Note that this approach would likely cause major economic damage to the Russian energy sector and its economy as a whole.

Third and building off this approach, Congress could go further and impose secondary sanctions on any financial institutions doing business with these Russian entities. Such a step would cut these entities off not only from the U.S. financial sector but would also limit their access to other markets as well. It would also likely limit their access to Chinese and other forms of financing. While wielding such a tool might cause a change in Russian behavior, it would also likely cause significant damage to the Russian economy and cause a serious diplomatic row with our European allies, which have been working closely with the United States in ramping up the pressure on Russia.

When evaluating these various proposals, two additional considerations merit attention. The first is the likelihood—and severity—of Russian countersanctions or other responses. As a result of U.S. and EU sanctions on Russia in response to its activities in Ukraine, Moscow imposed countersanctions on the EU, limiting food shipments.<sup>68</sup> The United States and the European Union should expect further symmetric and asymmetric responses in the case that we ramp up sanctions pressure. Such responses could include countersanctions or increased cyber activity, and could be proportional to degree of new pressure we impose on Moscow (*i.e.*, the more powerful sanctions we impose, the more significant Moscow's retaliation may be).

The second consideration is that while Russia poses many challenges to the United States, we still want the opportunity work with Moscow on a range of difficult issues, such as international terrorism, North Korea's nuclear weapons and ballistic missile programs, stability in Afghanistan, and a number of other areas. Ramping up sanctions pressure on Russia may impact their willingness to work constructively with us on these matters. While increased pressure is justified in response to Moscow's continued defiance of international law and aggressive actions towards the United States, we should recognize that further sanctions may make cooperation with Russia in other areas more difficult.

#### IV. Ensuring Russian Compliance

As this Committee considers imposing additional sanctions on Russia, it should also consider how to effectively unwind this pressure in such a way that provides Russia with the incentive to change its behavior. One of the key sanctions lessons of the past few years is that unwinding sanctions is

<sup>68</sup> "Russia May Extend Counter-Sanctions Until End-2017," *Reuters*, May 27, 2016, <http://www.reuters.com/article/us-russia-crisis-sanctions-idUSKCN0Y11GI>.

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often significantly more difficult than simply turning a legal switch.<sup>69</sup> Indeed, unwinding sanctions can often prove complicated, and in many cases ill-considered or ineffective blunt unwinding of sanctions provides unnecessary concessions to our adversaries and forgoes opportunities to continue to pressure these targets for a variety of other malign activities.<sup>70</sup> Likewise, ramping up powerful sanctions but failing to provide realistic pathways for countries to change their behavior and enjoy even partial sanctions relief could lead to a situation of sanctions stalemate, where the United States has imposed powerful sanctions but the target is unwilling to abide by every one of our demands (and therefore does not see any relief). Such a situation can be highly problematic, as the target suffers but the United States does not achieve its policy goals.

Aggressive sanctions ramp-up must be coupled with a thoughtful unwinding process, one that provides for meaningful relief to a target *if* that target changes its behavior and one that does not raise the bar for achieving such relief too high.

In certain respects, elements of the current legislative proposals in the Senate may raise the bar for relief too high. For example, Section II of the Countering Russian Hostilities Act—which imposes sanctions on Russia for its activities in Ukraine—sets a high threshold for termination of the sanctions program, namely that Russia ceases ordering, controlling, or otherwise supporting or financing separatist elements in Ukraine and also halts military operations in Syria. While the United States should seek to achieve these goals, most Russia analysts have doubts as to whether Russia will fully relinquish control of Crimea or totally cease military operations in Syria as a result of sanctions pressure. Yet in order for the sanctions to be lifted, that is what is required. Setting the bar for termination of these programs this high means that it is unlikely the United States will be able to unwind these sanctions in the foreseeable future.

Further, such a threshold actually disincentivizes Russia from even partially complying with many of its obligations under Minsk II; if the only way Russia can secure sanctions relief is with total fulfillment of its obligations under Minsk II, it has limited incentive to fulfill only some of its obligations, as it will be unlikely to see sanctions relief from doing so.

While the waiver elements of this legislation do provide for some flexibility—namely permitting the President to waive the imposition of certain sanctions if he determines it is in the national security interests of the United States and certifies that Russia is taking certain steps in Ukraine and Syria—what is needed is a statutorily constructed set of “**off-ramps**” that provide a clear roadmap for the Russians to receive limited sanctions relief in exchange for meeting certain obligations under Minsk II or verifiably reducing their malicious cyber activities against the United States and its partners.

<sup>69</sup> See, e.g., Peter Feaver and Eric Lorber “Penalty Box,” *Foreign Affairs*, June 6, 2014, <https://www.foreignaffairs.com/articles/united-states/2014-06-06/penalty-box>.

<sup>70</sup> Eric Lorber, “Securing American Interests: A New Era of Economic Power,” *Center on Sanctions and Illicit Finance, Foundation for Defense of Democracies*, Feb. 2017, [http://www.defenddemocracy.org/content/uploads/documents/CSIF\\_Securing\\_American\\_Interests.pdf](http://www.defenddemocracy.org/content/uploads/documents/CSIF_Securing_American_Interests.pdf).

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Such a statutory construct could work as follows: New legislation could include the codification of the Executive Orders related to Russia and Ukraine, along with additional, statutory designations of certain parties (*e.g.*, in an annex) involved in destabilizing Ukraine or currently governing Crimea. The legislation could further specify that these additional designations will be lifted if Congress reviews and agrees that Russia has fulfilled certain, delineated obligations under Minsk II. For example, if Russia withdraws all of its heavy weapons from the conflict zone, the United States will lift these designations. The level of sanctions unwinding provided could be queued to the magnitude of the obligation Russia fulfills. For example, if the new legislation includes powerful sanctions related to Russian sovereign debt, the lifting of those sanctions could be tied to the fulfillment of other, more significant obligations under Minsk II, such as Russia allowing for full Ukrainian control over its border with Russia throughout the conflict zone. In this way, the United States would not be providing significant sanctions relief to Russia in exchange for minor concessions.

Such legislation could be structured in alternative ways that achieve the same effect, as well. For example, the legislation could rely on a presidential certification that Russia had fulfilled certain of its obligations under Minsk II or that it had significantly reduced its cyber-attacks against the United States and its partners, but then provide Congress the opportunity to review and approve (or disapprove) of that certification following briefings by the administration and the intelligence community. Only upon approval would the statutorily imposed sanctions specified be unwound.

Any such provisions should include a degree of built-in flexibility, such as specifying that if Congress deems it appropriate, additional or alternate sanctions can be relaxed as a result of Russian actions. Such flexibility will ensure that while Congress demarcates a clear path in from the cold to Moscow, it can adjust to changes in the situation as necessary.

This “off ramp” approach provides a number of important benefits. First, it increases the likelihood that the United States will achieve some—albeit not all—of its objectives, particularly with regard to Ukraine. By ramping up pressure on Moscow and then providing such off-ramps, the United States will give Russia a clear path to sanctions relief and will increase the prospects that Moscow will live up to at least some of its Minsk II obligations. Otherwise and based on the current sanctions stalemate, it does not appear likely that Russia will change its activities in Ukraine and indeed may simply try to wait out U.S. sanctions until the parallel EU sanctions regime falls apart or with the hope that the Trump Administration will make a decision to relax some of the current sanctions on Russia.

Second, while providing limited sanctions relief, this approach also keeps the pressure on Russia to change its other undesirable behavior. While Russia may receive such limited relief, it will still be under significant economic pressure, particularly if some of the more powerful sanctions on the country remain in place. As a result, the United States can continue to pressure Russia even while granting it some relief. This approach overcomes one of the primary critiques of a major recent sanctions unwinding episode—the Joint Comprehensive Plan of Action (“JCPOA”) between the P5+1 and Iran. In that case, the Obama Administration was arguably reluctant to enforce remaining sanctions on Iran for fear of undermining the agreement, and as critics of the deal argue,

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partially as a result Iran continued to engage in destabilizing activity throughout the region, including exporting terrorism, ballistic missile development, and supporting Syrian President Bashar al-Assad and the Houthis in Yemen. Utilizing this “off ramp” mechanism may help avoid this pitfall by making it clear that a number of sanctions on Russia will remain in place even with the partial relief and that Russia should not expect to see relief related to those remaining sanctions unless and until it changes its behavior tied directly to them.

#### **V. Moving Forward**

Russia continues to threaten U.S. national interests in a number of ways, including its destabilizing activities in Ukraine and its cyber-attacks aimed at undermining democratic institutions, to say nothing of its blatant human rights abuses and brutal military campaign in Syria. The United States should be prepared to use all the tools at its disposal—diplomatic, cyber, economic, and military—to counter these Russian threats. But as Congress, which has a key role to play in these efforts, decides whether to ramp up economic pressure on Russia, it should do so in a way that is both responsible and provides Moscow with a clear pathway for drawing down tensions and gradually relieving that economic pressure as a reward for improved behavior.

Thank you for your time. I look forward to your questions.

**PREPARED STATEMENT OF RODNEY D. LUDEMA, Ph.D.**

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MARCH 15, 2017

**Introduction**

Chairman Crapo, Ranking Member Brown and distinguished Members of the Committee, thank you for the opportunity to testify at today's hearing assessing U.S. Sanctions on Russia. My name is Rodney Ludema, and I am a professor of economics at Georgetown University. Earlier this year, my co-author Daniel Ahn and I published a report titled, "Measuring Smartness: Understanding the Economic Impact of Targeted Sanctions,"<sup>1</sup> and I would like to take the opportunity to share some of its conclusions.

As you know, Russia's intervention in Ukraine in early 2014 prompted the United States and the European Union to impose series of "smart" sanctions—sanctions against specific individuals and companies, primarily in Russia and Ukraine. The sanctions began in March 2014, and the list of targets has grown steadily, now affecting several hundred companies explicitly and thousands more by association. Our study seeks to understand just how "smart" these sanctions have been in practice. That is, have they hit the intended targets with minimal collateral damage? We find that, with a few notable exceptions, the sanctions have inflicted significant damage on the intended targets, with relatively little short-run impact on the overall Russian economy.

**Smart Sanctions in Context**

While broad economic sanctions and trade embargoes have long been used as instruments of foreign policy, targeted sanctions focusing on specific individuals, companies, and transactions are relatively new. They are an outgrowth of a recognition that the effectiveness of an economic sanction in gaining compliance from a target government does not depend on the overall economic damage the sanction causes but on whether the target government itself and its key domestic constituencies feel the economic pain from noncompliance. Thus, sanctions are considered "smart" if they target responsible parties while minimizing collateral damage. For this reason, assessing the smartness of targeted sanctions on Russia is essential to assessing their efficacy.

Clouding the picture, however, is the fact that the conflict in 2014 roughly coincided with a series of powerful macroeconomic shocks, especially a dramatic decline in the price of oil (Russia's main export), which jolted both the Russian and world economies. The Russian economy slowed dramatically in 2014 and entered recession in 2015. This makes it difficult to determine with the naked eye whether the poor economic performance of a sanctioned company is due to sanctions or to the broader economic problems of the country. Likewise, it is difficult to determine whether the broader economic problems of the country are due to the oil shock or to collateral damage from sanctions.

The difficulty inherent in attributing Russia's poor economic performance following sanctions to a single cause has allowed for a wide range of conflicting claims regarding the economic costs of the sanctions to Russia and to neighboring economies. Opponents of sanctions, in particular, claim that sanctions have caused little pain to the specific targets, while inflicting untold economic damage on the Russian people and on neighboring countries (principally members of the European Union).

**Effects on Sanctioned and Associated Companies**

The first part of our study examines whether the sanctions impacted the intended targets. We assemble all companies listed on the Specially Designated Nationals and Blocked Persons (SDN) List and Sectoral Sanctions Identifications (SSI) List, along with all companies associated with individuals on the SDN list. Together with overlapping targets from a similar set of sanctions by the European Union, this comprises 584 unique targets. (In continuing research, we have also considered some 2,000 subsidiaries of these targeted companies and found similar results.)

Our method is to compare the performance of sanctioned companies to that of nonsanctioned peer companies before and after the sanctions were imposed. As sanctioned and nonsanctioned companies all face the same macroeconomic environment, comparing the two groups is a way to isolate the effect of sanctions. Our main

<sup>1</sup>The public link to the report can be found at <https://www.state.gov/documents/organization/267590>.

finding is that sanctioned companies are indeed harmed by sanctions relative to their nonsanctioned peers. On average, a sanctioned company loses an estimated:

- one-third of its operating revenue
- over one-half of its asset value
- about one-third of its employees

after being targeted compared to nonsanctioned companies. These estimates, which are large and appear highly statistically robust, suggest targeted sanctions do have a powerful impact of the targets themselves.

Beyond the broader strategic implications, these sanctions may therefore be tactically impairing the ability of the Russian Federation through these companies to further the illegal annexation of Crimea and the ongoing crisis in Eastern Ukraine.

### Macroeconomic Impacts

The second part of our study examines collateral damage. In particular, we consider the impact the sanctions have on Russian GDP and on its imports from the European Union. In contrast to the firm-level approach, it is not possible to cleanly separate out the effect of sanctions from the effect of other macroeconomic factors in the aggregate analysis. Instead, we pose a much simpler question: How much of the post-sanction performance of the Russian economy can be explained either directly or indirectly by falling oil prices?

The world oil price (Brent) fell from over \$100 in 2013 to under \$60 by the end of 2014, and declined further in the second half of 2015. A common rule of thumb for oil exporters suggests a \$40 drop in the world price of oil should shrink energy-dependent Russia's GDP by 4 to 5 percent. Indeed, we find that the oil price change explains the vast majority of the decline in Russia's GDP and import demand, with very little left to be explained by sanctions or other factors. We conclude that either sanctions had only a small negative effect on Russia's GDP or other positive factors largely canceled out the effect of sanctions.

There is good reason to believe that sanctions have had only a small negative macroeconomic effect in the first 2 years of their imposition. By far the largest companies on the sanctions list (energy companies, banks and defense companies, which make up a large fraction of the Russian economy) were not subject to blocking sanctions. Rather, they were subject to limitations on long-term borrowing and new technologies that, by design, should have a delayed effect. The reason for this design was to mitigate the potential negative impacts on U.S. companies and those of our allies.

As for positive factors that may have countered the effect of sanctions, the most plausible candidate factor would be the Russian policy response. Notable policy responses were the large depreciation of the Ruble in 2014, and government bailouts certain "strategic" firms. The government of Russia designates certain firms as strategic because of their economic and national security importance to be prioritized to receive state largess in the form of state loans guarantees, capital participation, more government contracts, and tax breaks. It is important to note that such policy responses are costly to the Russian government, and thus this constitutes an indirect avenue by which the sanction effect is felt.

Finally, we find that sanctions have had a small effect on the economies of most EU countries. Adding together the impacts of sanctions and Russia's agricultural countersanctions on EU exports gives a median impact across EU countries of just 0.13 percent of GDP (though with considerable variation across the EU members). The reasons for this are: (1) Russia generally accounts for a small share of total EU countries' exports; and (2) most of the decline in Russian imports is explained by lower oil prices and trend factors.

### Conclusions and Implications for Future Sanctions

Economic sanctions are meant to signal international disapproval, deter further aggression, and create leverage in negotiations with the targeted country aimed at reversing the offending policies. Whether the current set of sanctions against Russia will ultimately accomplish these goals is unknown, but good sanctions design gives the United States and its allies the best chance of success.

History teaches that sanctions are most effective when they are multilateral, sustainable, focused, and clearly contingent on an achievable goal. The current sanctions on Russia were designed with these principles in mind. While not fully multilateral, they include the European Union, which is a region of great importance to the Russian economy. They were designed to cause minimal collateral damage in the short term and thus have proven sustainable so far. Our study largely confirms the success of this design element. Any new sanctions, if targeted at the broader



Russian economy, could easily cause collateral damage and thus should be approached with caution. The current sanctions were designed to focus their impact on the companies and individuals involved furthering Russia's illegal annexation of Crimea and ongoing Ukraine policy. Our study largely confirms the success of this design aspect as well. Any new sanctions targeting different policies should be similarly targeted.

Finally, current sanctions are contingent on certain Minsk II milestones, and while they have yet to be reached, they are clear. Sanctions policies that tie the hands of negotiators in such a way as to prevent achieving the goal should be avoided.

**RESPONSE TO WRITTEN QUESTION OF SENATOR TOOMEY  
FROM ERIC B. LORBER**

**Q.1.** Following the imposition of sanctions, many Russians may have believed that sanctions were a cause of Russia's economic downturn. How could sanctions be better targeted to restrict Russia's capabilities without encouraging anti-American sentiment?

**A.1.** Sanctions that focus on Russian President Vladimir Putin and his cronies' corruption could be particularly effective at putting pressure on Russia while not encouraging anti-American sentiment.

President Vladimir Putin is adept at manipulating state-controlled media sources to put the blame for Russia's economic struggles squarely on Western sanctions. While factually untrue, large swaths of the Russian population believe the United States is the cause of the economic anguish they feel. Additional, broad-based sanctions that target Russia's economy or particular sectors within that economy (such as sectoral sanctions) may exacerbate this problem, and while putting additional pressure on Vladimir Putin, may also increase anti-American sentiment within Russia.

Sanctions—and sanctions-like tools—could be better targeted to pressure Russia's elites and ruling class while limiting the impact on the Russian population more generally. One way to do this—as I mentioned in my written testimony—would be to identify, track, and as appropriate, seize assets of sanctioned Russian elites in the United States and in certain foreign jurisdictions.

Russian oligarchs are well known to launder money coming out of Russia through high-end real estate purchases in urban centers, often paying cash for these properties. Recently, the Financial Crimes Enforcement Network at the United States Department of the Treasury has collected information related to high-end real estate purchases by anonymous parties through its recent Geographic Targeting Order.<sup>1</sup> It is widely believed that FinCEN's information collection has produced substantial relevant information on these flows and where some of these individuals' assets are. Identifying these assets in the United States and partner jurisdictions (such as the United Kingdom, where Russian oligarchs have purchased large amounts of luxury real estate in London) and seizing them if necessary (*e.g.*, if they belong to designated Russian persons) could put additional pressure on individuals within Vladimir Putin's circle of cronies in ways that would not directly impact common Russians.

An additional benefit of such action would be that it directly plays into one of the primary grievances ordinary Russians do have

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<sup>1</sup> See, *e.g.*, "FinCEN Renews Real Estate 'Geographic Targeting Orders' to Identify High-End Cash Buyers in Six Major Metropolitan Areas," *Financial Crimes Enforcement Network Press Release*, Feb. 23, 2017, available at <https://www.fincen.gov/news/news-releases/fincen-renews-real-estate-geographic-targeting-orders-identify-high-end-cash>.

against the Putin government and Russia's oligarchs more broadly: corruption. As recent street protests have illustrated, significant elements in Russia are frustrated with the substantial level of corruption at the highest levels of government.<sup>2</sup> To the extent that U.S. sanctions and sanctions-like measures focus on the Russian elites' corrupt activities, they will in turn be less likely to produce anti-American sentiment. Congress should therefore consider focusing its legislative authority on measures—such as setting up a Russian corruption task force at FinCEN—that target Russian corruption and that freeze illicit Russian assets in ways that hurt the bank accounts of key Russian oligarchs. While such a task force would put pressure on Putin and his cronies, Congress should remain clear eyed that such measures—while powerful—would be unlikely to change Russian activity if not situated as part of a well-developed strategy using all means of U.S. statecraft.

#### RESPONSE TO WRITTEN QUESTION OF SENATOR TILLIS FROM ERIC B. LORBER

**Q.1.** Can you please outline what a sustained regimen of Russia sanctions might look like. I am interested in your opinions on what an idealized sanctions framework looks like, one where the United States potentially has a multilateral engagement with EU or NATO partners, so that we move toward a goal of isolating Russian leaders (oligarchs? Putin's cronies?) and bad actors as opposed to harming innocent Russian civilians. What concrete policies could the United States put in place that would make Russian leaders start to produce a mutually beneficial behavior over the long term? How does U.S. energy policy influence the ability of the United States and other nations to exercise effective sanctions?

- Please outline a framework and strategy for exercising and implementing incremental and sustainable sanctions, and what other policy tools should be used to couple sanctions. At what point is an escalation of engagement appropriate? What are the next steps when sanctions and other diplomatic avenues in controlling malign activities? How do you counteract negative messaging about sanctions in Russia—to win the hearts and minds of individuals in Russia?

**A.1.** One of the core tenets of a sustainable sanctions program to effectively pressure Russia is close U.S. and EU cooperation. The EU sanctions have been instrumental in ensuring that Russia cannot offset much of the economic pain imposed by U.S. sanctions. To the extent that the United States and European Union can continue to closely coordinate their sanctions programs, those programs will be more effective. Any new U.S. sanctions should—at the very least—take into account whether the European Union will be willing to join with its own regulations.

With that as background, an idealized sanctions program is one that gradually ramps up the pressure on Russia and in particular on Russian oligarchs and cronies, specifically by targeting their

<sup>2</sup>Andrew Higgins, "Aleksei Navalny, Top Putin Critic, Arrested as Protests Flare in Russia," *New York Times*, Mar. 26, 2017, available at [https://www.nytimes.com/2017/03/26/world/europe/moscow-protests-aleksei-navalny.html?\\_r=0](https://www.nytimes.com/2017/03/26/world/europe/moscow-protests-aleksei-navalny.html?_r=0).

corrupt activities. Such gradual pressure—where the United States tightens the vice slowly but deliberately—will be significantly more likely to achieve EU buy-in than a fast, powerful escalation of sanctions (such as imposing broad import restrictions on Russian energy products). Likewise, such gradual and deliberate pressure can help U.S. diplomats make the case for additional sanctions; if Russia refuses to change its behavior as a result of limited escalation, the United States can argue to our European counterparts that more means are necessary.

My written testimony lays out a number of options for incrementally increasing the pressure on Moscow, and I reproduce them at a high level here:

- The codification of certain executive orders (“EOs”), including EOs 13660, 13661, 13662, 13685, and 13694, as well as additional statutory designations under these codified EOs;
- Establishment of a task force, potentially led by the Financial Crimes Enforcement Network (“FinCEN”), to identify and seize assets of targeted Russian persons, including those with close ties to Russian President Vladimir Putin;
- Certain restrictions related to U.S. and European financial institutions’ purchase or facilitation of Russian sovereign debt, which has been a way for Russia to prop up Russian state-owned enterprises and financial institutions in the face of sectoral sanctions; and
- Primary sanctions on elements of Russia’s oil and gas industry, with possible carve-outs for certain countries particularly dependent on the Russian energy sector.

Note that, as I explain in my response to Senator Toomey’s question above, the FinCEN task force and its focus on Russian corruption may be the tool least likely to engender anti-American sentiment. Most of the more powerful sanctions options will likely have macroeconomic effects on Russia’s economy, and Putin will be more able to use them for propaganda purposes.

In terms of coupling sanctions with other policy tools, these economic measures must be nested in a larger strategy of pressuring Moscow, including aggressive diplomacy and responding in kind to malign Russian activities such as offensive cyber operations. Sanctions are a means to an end, and Congress and the Administration must be clear as to what that end is and how they intend to achieve it. Ramping up economic pressure on Moscow without clear objectives, the employment of other coercive tools, and buy-in from the Administration—is unlikely to be effective in getting Moscow to change its behavior. While it imposes sanctions, the United States should be actively combating Russian aggression in cyber space, for example.

Finally, Congress should think through how it can unwind sanctions pressure in the case that Moscow—even partially—changes its behavior. Current sanctions bills, including the Counteracting Russian Hostilities Act of 2017 (“Counteracting Russian Hostilities Act”),<sup>1</sup> ramp up the pressure on Russia significantly. Yet, as we have learned over the past few years, unwinding sanctions can

<sup>1</sup>S. 94, “Counteracting Russian Hostilities Act of 2017,” 115th Cong. (2017).

often be a difficult and fraught process, and Congress should think about how and when it will unwind sanctions even as it builds pressure. Any such new sanctions legislation should include built-in “off-ramps”—namely elements of the sanctions regime, such as specific designations or specific Directives—that could be undone in a situation of partial Russian compliance with its various obligations, such as those under the Minsk agreements. Such partial sanctions relief could be traded for Russian fulfillment of these obligations, and this approach would increase the chances the United States could limit—though not completely eliminate—Russian challenges to U.S. interests. I have explained how to construct a sanctions framework that focuses on “smart unwinding” in my written testimony.