

House Permanent Select Committee on Intelligence

Putin's Playbook:
**The Kremlin's Use of Oligarchs,
Money and Intelligence in
2016 and Beyond**

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Chairman Schiff, Ranking Member Nunes, and distinguished members of the Permanent Select Committee on Intelligence, I am honored to appear before you today to discuss Putin's Playbook: The Kremlin's Use of Oligarchs, Money and Intelligence in 2016 and Beyond.¹ As an economic sanctions compliance and illicit finance professional, I will focus my testimony on the impact – and limits – of U.S. sanctions in countering Russia's continued malign activity. I will also discuss a number of additional measures that could be undertaken by the administration and Congress to limit the ability of Moscow and its cronies to surreptitiously move their funds and assets around the world.

As this committee knows well, Russia poses a serious national security challenge to the United States. In the last few years alone, Russia has illegally occupied Crimea; destabilized Ukraine through the use of the Russian military and its proxies; attempted to subvert Western democracies, including by attacking the integrity of U.S. elections; launched cyberattacks against the United States and our allies; supported the murderous Assad regime in Syria; and used chemical weapons to conduct assassinations in Western Europe, harming numerous civilians. The United States and its allies and partners must respond forcefully and thoughtfully to this threat, including through the use of targeted economic measures.

I will focus my testimony today on three key points. First, our sanctions on Russia have had an impact. Through the use of coercive economic measures, we have put pressure on particular Russian targets (including Russian oligarchs) and caused economic pain to the Russian economy writ large.

Second, this impact has been limited. While resulting in some changes in Russian behavior, existing sanctions are unlikely to significantly alter Russian decision making absent an escalation that would be costly to both our allies and partners in Europe and many in the private sector.

Third, we need to look beyond sanctions to additional economic measures. Such measures should include tracking, tracing, and preventing illicit Russian funds from entering the legitimate international financial system to counter certain types of malign Russian influence and activity, as well as to pressure corrupt actors within Russia. This requires strengthening the anti-money laundering/combating the financing of terrorism (AML/CFT) backbone of the international financial system to limit Russian illicit finance. But members of Congress and the administration should be cautious in relying too heavily on these economic tools. In recent years, sanctions and related tools have become the tool of first resort in addressing a range of Russian malign activity. While they are powerful, they must be properly situated in a strategic framework and used to complement other elements of national power.

The Current Sanctions Framework

The sanctions program targeting Russia is one of the most comprehensive sanctions programs currently administered by the United States. This program consists of all types of U.S. economic sanctions: a comprehensive jurisdictional embargo on the annexed Ukrainian region of Crimea; a

¹ The views expressed in this testimony are my personal views and do not represent the views of the Foundation for Defense of Democracies, the Financial Integrity Network, or the Treasury Department. Pursuant to legal and ethical obligations, I cannot discuss internal deliberations that occurred during my tenure at the Treasury Department.

list-based designation program targeting specific Russian persons, such as the so-called “oligarchs” and those engaged in corruption and human rights abuses; a sectoral sanctions program that limits certain types of transactions with key Russian economic sectors and entities; an export-control regime designed to prevent Russian firms from accessing American technology important to the development of the Russian energy sector; and a secondary sanctions program on foreign firms doing business with malign Russian actors in the defense and intelligence sector or with Russian specially designated nationals (SDNs).

Combined with EU sectoral sanctions, a list-based designation program, and export control restrictions, our sanctions on Russia are designed to target individuals and entities closely associated with the Putin regime, impose economic pain on key sectors of the Russian economy, and impact the long-term growth of certain Russian industries through limiting key financing and access to technology.

Like the Obama administration, the Trump administration has relied heavily on economic pressure as a way to counter Russia’s range of malign activities. To date, the Trump administration has sanctioned more than 270 Russia-related individuals and entities, including a set of designations on April 6, 2018 that targeted key Russian oligarchs close to Russian President Vladimir Putin who are engaged in illicit activity, as well as companies they own and control. The administration has also targeted Russian companies and financial institutions involved in sanctions evasion, including for their efforts to support Nicholas Maduro’s illegitimate regime in Venezuela and to provide support to North Korea, Syria, and Iran. As Treasury Under Secretary Sigal Mandelker noted in testimony in August 2018, the Russia sanctions program is among Treasury’s most active; through it, both Congress and the Treasury Department have imposed major costs on Russia.²

As part of its efforts to impose economic costs on key Russian actors for their malign activities, the Treasury Department has not shied away from targeting large and important Russian companies. Beyond the sectoral sanctions designations put into place by the Obama administration that imposed debt and equity restrictions on important Russian energy, financial, and defense companies – which Congress tightened with the passage of the Countering America’s Adversaries Through Sanctions Act (CAATSA) – the Treasury Department has targeted major Russian-owned companies. This includes EN+ Group, UC Rusal, and JSC EuroSibEnerg, which were owned or controlled by Oleg Deripaska, a Russian national designated for allegedly “threatening the lives of business rivals, illegally wiretapping a government official, and taking part in extortion and racketeering” as well as being close to the Russian State and Vladimir Putin.³ Just two weeks ago, for example, Treasury sanctioned Evrofinance Mosnarbank, a Moscow-based bank that is jointly owned by Russian and Venezuelan state-owned companies (including Russian Bank VTB owning a 25 percent stake),

² Treasury Under Secretary Sigal Mandelker, *Statement before the U.S. Senate Committee on Banking, Housing, and Urban Affairs*, August 21, 2018. (<https://home.treasury.gov/news/press-releases/sm465>)

³ U.S. Department of the Treasury, Press Release, “Treasury Designates Russian Oligarchs, Officials, and Entities in Response to Worldwide Malign Activity,” April 6, 2018. (<https://home.treasury.gov/news/press-releases/sm0338>)

for, among other things, providing financing for the illicit Venezuelan cryptocurrency, the Petro.⁴

The Effectiveness – and Limits – of U.S. Sanctions on Russia

U.S. and EU sanctions have had both macroeconomic and targeted impacts. During the initial phase of the sanctions during the Obama administration, the Russian economy clearly struggled, 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 (CRS) noted that most sanctions hit just as the oil price was dropping by more than 60 percent between the start of 2014 and the end of 2015.⁵ Yet the sanctions did appear to have an independent impact at the macroeconomic level. A 2015 IMF study estimated 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%.”⁶ 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 2015.⁷ Likewise, in 2016, Putin noted that sanctions were harming Russia’s access to international financial markets.⁸

In recent years, however, the Russian economy has stabilized. According to CRS, as oil prices began to rise in 2016, “[t]he rate of economic contraction slowed, inflation fell, and the value of the ruble stabilized. The Russian government and non-sanctioned Russian entities resumed some access to international capital markets, capital outflows slowed, and foreign direct investment into Russia rebounded.”⁹ Overall, the sanctions appeared to have had a modest, but negative, impact on the Russian economy, though the economy is in significantly better shape now than it was when the sanctions were first imposed.¹⁰

Those targeted directly by U.S. sanctions have also felt their bite. As noted by Assistant Secretary of the Treasury for Terrorist Financing and Financial Crimes Marshall Billingslea:

According to public reporting, the combined net worth of Russia’s 27 wealthiest people fell by an estimated \$16 billion in one day [after the April 6 oligarch designations], Moscow-traded stocks had their biggest drop in four years, and the ruble fell to its weakest position since late 2016. Viktor Vekselberg’s net worth

⁴ U.S. Department of the Treasury, Press Release, “Treasury Sanctions Russia-based Bank Attempting to Circumvent U.S. Sanctions on Venezuela,” March 11, 2019. (<https://home.treasury.gov/news/press-releases/sm622>)

⁵ Rebecca Nelson, “U.S. Sanctions and Russia’s Economy,” *Congressional Research Service*, February 17, 2017. (<https://fas.org/sgp/crs/row/R43895.pdf>)

⁶ *Ibid.*, pages 6-7.

⁷ Ed Adamczyk, “Medvedev: Sanctions cost Russia \$106 billion,” *UPI*, April 22, 2015.

(http://www.upi.com/Top_News/World-News/2015/04/22/Medvedev-Sanctions-cost-Russia-106-billion/3551429721857)

⁸ Nikolaus Blome, Kai Kiekmann, and Daniel Biskup, Interview with Putin, *Bild*, November 1, 2016.

(<https://www.bild.de/politik/ausland/wladimir-putin/russian-president-vladimir-putin-the-interview-44092656.bild.html>)

⁹ Cory Welt, Kristin Archick, Rebecca Nelson, and Dianne Rennack, “U.S. Sanctions on Russia,” *Congressional Research Service*, January 11, 2019, page 42. (<https://fas.org/sgp/crs/row/R45415.pdf>)

¹⁰ *Ibid.*, page 44.

has dropped an estimated \$3 billion, and foreign governments have launched investigations in response to his designation and subsequently frozen Vekselberg's assets in their jurisdictions. Vekselberg's Renova Group was forced to divest from ventures in Switzerland and Italy.¹¹

While sanctions on Russia have had a macroeconomic impact and have caused pain for particular Russians close to Putin, their impact on Russian behavior appears more limited.

Some analysts believe that sanctions have had some impact on behavior because, in their absence, Russia would likely have acted more aggressively. Former 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."¹² 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. A March 2016 European Parliament publication argued that sanctions were deterring further violence, again pointing to the Black Sea port of Mariupol.¹³

In addition, at least in the context of Ukraine, Putin and Foreign Minister Sergei Lavrov explicitly called for, and even demanded, 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.¹⁴ 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 have impacted Russian decision making.

Nevertheless, Russia continues to engage in widespread malign activity. In recent years, Russia has continued its cyberattacks against Ukraine,¹⁵ Montenegro,¹⁶ and Western democracies, including efforts in 2017 to interfere with the French presidential election.¹⁷ Likewise, Russia is no closer to fulfilling its obligations under the Minsk Agreement and continues its destabilizing activities in a number of theaters around the world, including supporting the murderous Assad regime in Syria, using chemical weapons to conduct assassinations in Europe, and continually

¹¹ Treasury Assistant Secretary Marshall Billingslea, *Statement before the U.S. Senate Committee on Foreign Relations*, August 21, 2018. (<https://home.treasury.gov/news/press-releases/sm464>)

¹² Peter Harrell, "Lessons from Russia on the Future of Sanctions," *Center for a New American Security*, September 2015. (<https://s3.amazonaws.com/files.cnas.org/documents/CNAS-Report-Economic-Statecraft-2-FINAL.pdf>)

¹³ Martin Russell, "Sanctions over Ukraine: Impact on Russia," *European Parliamentary Research Service*, March 2016. ([http://www.europarl.europa.eu/RegData/etudes/BRIE/2018/614665/EPRS_BRI\(2018\)614665_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2018/614665/EPRS_BRI(2018)614665_EN.pdf))

¹⁴ "Putin Steps Up Drive to Kill Sanctions Amid Signs of EU Disunity," *Reuters*, July 29, 2016. (<http://www.voanews.com/a/putin-steps-up-drive-kill-sanctions-signs-eu-disunity/3440262.html>)

¹⁵ Natalia Zinets, "Ukraine charges Russia with new cyber attacks on infrastructure," *Reuters*, February 15, 2017. (<http://www.reuters.com/article/us-ukraine-crisis-cyber-idUSKBN15U2CN>)

¹⁶ Ben Farmer, "Montenegro Asks for British Help after Cyber Attacks in Wake of 'Russian-backed coup plot,'" *The Telegraph* (UK), February 28, 2017. (<https://www.telegraph.co.uk/news/2017/02/28/montenegro-asks-british-help-cyber-attacks-wake-russian-backed>)

¹⁷ "France drops electronic voting for citizens abroad over cybersecurity fears," *Reuters*, March 6, 2017. (<http://www.reuters.com/article/us-france-election-cyber-idUSKBN16D233?il=0>)

interfering in foreign elections, including in the United States.¹⁸ Indeed, through Department of Justice indictments, sanctions designations, and other public actions, the United States has publicly identified a number of Russian efforts to directly influence U.S. and Western European elections.¹⁹

Overall, it appears that our sanctions campaign has had a modest impact on the Russian economy and Russian decision making, but as currently conceived and implemented, and absent a significant escalation, it will be insufficient to counter the range of malign Russian activity.

Further, U.S. efforts to substantially escalate pressure on the Russian economy through sanctions and similar tools would likely come at substantial cost to U.S. allies and partners. For example, designating important Russian financial institutions as SDNs or targeting European companies participating in Nordstream II would have an impact on Russian firms and the Russian economy more broadly, but it would also have contagion effects in European markets, as well as potentially in U.S. markets. While such escalatory options are available to the United States, they also carry significant risks to U.S. interests.

Finally, there is ample reason to believe that Russia has likely planned contingencies and mitigation measures for addressing additional U.S. sanctions pressure. The United States has been ramping up and threatening additional economic pressure for almost five years, and many of the options before Congress (including designating particular Russian banks and prohibiting certain transactions in sovereign debt) have been under consideration since 2016. As one of my fellow witnesses mentioned in a recent report,²⁰ Russian illicit finance tactics have evolved significantly in the last few years, and it is likely that they have developed ways to blunt at least some of the impact of additional pressure.

Key Imperatives Moving Forward

To date, successive administrations have relied on sanctions as the primary response to continued Russian efforts to threaten U.S. interests. But we need to think more broadly and creatively about both what we are trying to achieve with our use of these tools and other, non-sanctions levers we have to counter Russian activity. In particular, Congress and the administration should work to bolster the AML/CFT regime here in the United States and among our allies, partners, and vulnerable jurisdictions abroad. Such an approach would have at least three significant benefits in the context of pushing back against Russian influence.

First, it would make our sanctions programs more effective. To the extent that U.S. and European financial supervisors, regulators, intelligence, and law enforcement agencies are better able to track, trace, and seize Russian financial flows and assets, our sanctions program will be more impactful. One of the primary challenges in any sanctions program is effective

¹⁸ For example, see: U.S. Department of Justice, Press Release, “Russian National Charged with Interfering in U.S. Political System,” October 19, 2018. (<https://www.justice.gov/opa/pr/russian-national-charged-interfering-us-political-system>)

¹⁹ “Fact Sheet: What We Know about Russia’s Interference Operations,” *Alliance for Securing Democracy*, March 25, 2019. (<https://securingdemocracy.gmfus.org/fact-sheet-what-we-know-about-russias-interference-operations>)

²⁰ Heather Conley, Donatienne Ruy, Ruslan Stefanov, and Martin Vladimirov, “The Kremlin Playbook 2,” *Center for Strategic and International Studies*, March 2019. (<https://www.csis.org/features/kremlin-playbook-2>)

implementation. While it is relatively easy to screen transactions, customers, and counterparties for names of SDNs, Russian oligarchs and sanctioned parties are adept at hiding their identities and involvement in efforts to move funds around the world. The real work to make these programs effective takes place when conducting investigations into the ultimate beneficial owners of companies, unmasking front and shell companies, and working to determine sources of funds. To the extent that the United States and its allies and partners bolster their AML/CFT regimes and the requirements they impose on financial institutions, the more likely financial institutions and other related entities are to detect and catch Russian illicit actors, including SDNs, trying to use their institutions to move illicit funds.

Second, as one of my fellow witnesses has made clear in a recent report, Russia uses these networks to exert influence in Eastern and Western Europe, including through supporting political parties and undermining democratic processes.²¹ To the extent that the intelligence agencies, regulators, law enforcement, and financial institutions are able to detect and shut down these networks, it will be more difficult for Russia to conduct such influence operations.

Third, such an approach would have the added, and important, benefit of bolstering our defenses against illicit financing more broadly. Many of the recommendations provided below would have beneficial impacts beyond countering specific Russian activity. For example, passing beneficial ownership legislation would not only make it more difficult for sanctioned Russian persons to move money into the United States, it would also make it more difficult for money launderers, drug kingpins, human traffickers, and many others to abuse the U.S. financial system.

To meaningfully disrupt these networks, Congress should take a number of actions:

- 1. Pass Meaningful Beneficial Ownership Legislation.** Russian oligarchs, money launderers, human traffickers, sanctions evaders, and other criminals have used front and shell companies to hide their true identities and move funds through the international financial system. As just one example, between 2011 and 2014, well-connected Russians used 5,140 shell companies that had accounts with 732 banks in 96 countries to move \$20.8 billion out of Russia in the so-called “Russian Laundromat Scandal.”²² Even as the United States continues to enhance and expand its financial tools and power to combat various national security threats, these efforts are increasingly undermined by exploitation of anonymous legal entities. For example, foreign adversaries can use anonymous companies for a range of purposes here in the United States, including undermining the efficacy of important laws such as the Foreign Agents Registration Act (FARA) and campaign finance laws. While it is important to push our allies, partners, and other jurisdictions to require companies to collect, maintain, and disclose accurate beneficial ownership information for certain legal entities at the time of company formation, we must also follow the same standard here in the United States and pass such legislation. This has been such an initiative in successive congressional sessions and

²¹ Ibid.

²² “The Russian Laundromat Exposed,” *Organized Crime and Corruption Reporting Project*, March 20, 2017. (<https://www.occrp.org/en/laundromat/the-russian-laundromat-exposed>)

Secretary of the Treasury Steven Mnuchin has likewise made clear that we need to figure out an efficient and prudent way to have access to beneficial ownership information.²³

- 2. Resource Implementation and Enforcement.** The AML/CFT/sanctions apparatus in the U.S. government is small and the budget spartan given the outsized role that the professionals at Treasury and relevant law enforcement and regulatory agencies are asked to play in safeguarding national security. Compared with the hundreds of billions of dollars provided to the Department of Defense each year, the Office of Terrorism and Financial Intelligence (TFI) at the Treasury Department – which houses the Office of Foreign Assets Control (OFAC), the Financial Crimes Enforcement Network (FinCEN), and an in-house intelligence agency, along with a policy shop – has a FY 2019 budget of approximately \$141 million (with a request for approximately \$166 million in FY 2020).²⁴ The professionals at TFI each handle elements of multiple programs, work very long hours, and are asked to do more than their fair share. Given that Treasury is being asked to address an ever-growing set of national security challenges, Congress should provide TFI with significantly increased resources to ensure it is able to address the challenges at hand. Note that this should also include proper resourcing for other offices and agencies engaged in this mission. Proper resourcing is critical in ensuring that our tools remain sharp.
- 3. Call Upon FinCEN to Issue an Advisory on Russian Sanctions Evasion and Money Laundering Red Flags.** FinCEN regularly promulgates guidance to U.S. financial institutions related to illicit finance risks and red flags associated with particular jurisdictions, customer types, and products and services. Recent advisories have highlighted corruption-related risks in Venezuela, red flags associated with Iranian sanctions evasion activity, and North Korean efforts to access the international financial system. To assist U.S. financial institutions in tracking, tracing, and disrupting illicit Russian financial flows, Congress should call upon the Treasury Department to issue a FinCEN advisory that details red flags associated with Russian illicit fund flows. Such an advisory would help enlist financial institutions in U.S. efforts to combat this illicit activity. In addition, Congress could also call upon FinCEN to coordinate such an advisory with its international partner financial intelligence units (FIUs) as part of the Egmont Group. An internationally coordinated advisory would further assist foreign financial institutions in detecting and preventing abuse of their institutions by illicit Russian actors.
- 4. Call Upon FinCEN to Publicly Identify Jurisdictions of Russian Money Laundering and Sanctions Evasion Concern.** Relatedly, Congress should call upon FinCEN to publicly identify particular jurisdictions that pose significantly higher risks of Russian money laundering and sanctions evasion concerns. Under Section 311 of the USA PATRIOT Act, FinCEN has the authority to identify financial institutions and

²³ Samuel Rubinfeld, “Mnuchin Seeks Shell Company Changes Within Six Months,” *The Wall Street Journal*, July 12, 2018. (<https://blogs.wsj.com/riskandcompliance/2018/07/12/mnuchin-seeks-shell-company-changes-within-six-months>)

²⁴ U.S. Department of the Treasury, “Congressional Budget Justification and Annual Performance Report and Plan: FY 2020,” accessed March 25, 2019. (<https://home.treasury.gov/system/files/266/06.-TFI-FY-2020-CJ.pdf>)

jurisdictions as primary laundering concerns and require that U.S. financial institutions impose a range of restrictions when conducting transactions and business with financial institutions incorporated in those jurisdictions. While a Section 311 jurisdictional identification may not be warranted in many cases, FinCEN, along with certain partner FIUs around the world, could publicly identify jurisdictions of higher risk for Russian sanctions evasion and money laundering, including providing specific information on the types of activities that have occurred within those jurisdictions. This would put financial institutions on notice for these red flags and take extra precautions when doing business with entities based in these jurisdictions.

- 5. Encourage Treasury to Target Russian Sanctions Evasion Networks.** OFAC has targeted a number of Russian sanctions evasion schemes in recent months, including a Russian financial institution's efforts to prop up the Maduro regime²⁵ and an international network through which the Iranian regime, working with Russian companies, provides millions of barrels of oil to the Syrian government.²⁶ In addition to making it more difficult for these networks to effectively operate, these actions have the additional benefit of highlighting Russian evasion tactics and making it clear to those in the public and private sectors around the world how Russian individuals and entities are attempting to undercut sanctions. OFAC's efforts to target these types of networks should be encouraged as a way to both roll up these networks and to provide important information that the private sector can use to bolster their sanctions and AML/CFT systems and controls, hardening the international financial system against abuse. Likewise, this committee should encourage OFAC to even more aggressively use its authorities to target key financial and commercial conduits and intermediaries between illicit actors and rogues, such as Russia, Venezuela, Iran, and others.

- 6. Consider Ways to Broaden the Aperture of Sanctions Targeting Russian Intelligence Services.** OFAC has already designated the GRU and the FSB, and secondary sanctions apply to certain foreign persons knowingly conducting significant transactions with these entities pursuant to CAATSA. OFAC should be encouraged to use these baseline designations as a platform for an operational sanctions program that aims to expose and disrupt continued Russian influence operations here in the United States and abroad. OFAC has significant experience using baseline designations to successfully build out a program targeting a network of malign actors and activity – a good example is the U.S. targeting of the Iranian Revolutionary Guard Corps (IRGC) and the focus on many of the entities it supports (and those supporting it) as part of the U.S. Iran sanctions program. Such a derivative campaign against Russian intelligence operations could increase the cost of their intelligence operations and also expose significant elements of their efforts to influence elections, undercut democratic processes, and otherwise engage in threatening activity.

²⁵ U.S. Department of the Treasury, Press Release, "Treasury Sanctions Russia-based Bank Attempting to Circumvent U.S. Sanctions on Venezuela," March 11, 2019. (<https://home.treasury.gov/news/press-releases/sm622>)

²⁶ U.S. Department of the Treasury, Press Release, "Treasury Designates Illicit Russia-Iran Oil Network Supporting the Assad Regime, Hizballah, and HAMAS," November 20, 2019. (<https://home.treasury.gov/news/press-releases/sm553>)

Conclusion

Increased transparency, additional sanctions, and cooperation with allies and partners on additional economic pressure can have an impact on Vladimir Putin's cronies and the Russian regime's willingness and ability to threaten U.S. interests. But while these tools are powerful, this committee, Congress, and the administration more generally should not labor under the misconception that our economic authorities alone are a silver bullet to counter Russia's malign activities. I would be happy to discuss any of the particular recommendations I have put forth, as well as sanctions on Russia more broadly.

Thank you and I look forward to your questions.