

Keeping Sanctions “Smart”: Calibrating U.S. Sanctions Policy to Overcome Overcompliance

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Abstract:

As U.S. sanctions programs have increased in breadth and multiplied in number, companies have in recent years taken significant steps beyond those required by U.S. law to de-risk their operations, concluding that they are better off avoiding any exposure to potential enforcement actions by U.S. regulators on account of U.S. sanctions violations. The U.S. government did not forecast this at times overly cautious approach, the results of which have conflicted with or undermined U.S. foreign policy goals. This Article examines the legal framework of U.S. sanctions authorities, including its principal mechanism of outsourcing key elements of U.S. national security policy implementation to private sector entities, analyzes the incentives those entities face in turn to “overcomply,” and addresses the challenges these developments present to U.S. national security objectives, including the negative byproducts of unmandated enforcement and other forms of corporate “self-sanctioning” and overcompliance. It concludes by proposing steps U.S. authorities can take in order to mitigate overcompliance. The Article highlights the complications that arise when a critical component of the U.S. national security architecture is outsourced to the private sector, and it suggests that this development may necessitate new forms of guidance and close cooperation between U.S. officials and corporate entities in order to ensure U.S. sanctions programs are effectively calibrated to achieve their policy objectives.

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I. Introduction: The Overcompliance Dilemma

Sanctions play an increasingly central role in U.S. national security policy, often serving as a tool of first resort that stands in

the place of more traditional kinetic national security responses.¹ Made possible principally by the primacy of the U.S. dollar in international trade, the United States Treasury Department, and in particular the Department's Office of Foreign Assets Control ("OFAC"), which both implements and enforces U.S. sanctions policy,² has especially since September 11, 2001, pursued a policy of "smart" sanctions that is designed to coerce foreign adversaries and cut off terrorist and other illicit actors from the global financial system while limiting the negative impact of such measures on innocent third parties.³

In recent years, the issue of overcompliance with U.S. sanctions has risen to the forefront of discussions regarding the purpose, effectiveness, and architecture of U.S. sanctions.⁴ These debates have primarily addressed overcompliance from two angles. The first observes what some scholars call the "extraterritoriality" of U.S. sanctions, and the decision of non-U.S. firms to not only comply with U.S. sanctions requirements, but to go beyond them, effectively de-banking and isolating U.S. sanctions targets as well as third parties located within a particular jurisdiction or segment of a target state's economy.⁵ Other literature, as well as policy statements, address the negative humanitarian impact overcompliance can have when U.S. and non-U.S. firms refuse to

¹ Johnpatrick Imperiale, *Sanctions by the Numbers: U.S. Sanctions Designations and Delistings, 2009-2019*, CTR. FOR A NEW AM. SEC. (Feb. 27, 2020), <https://www.cnas.org/publications/reports/sanctions-by-the-numbers> [https://perma.cc/SF8W-BXT2] (reporting an increased number of sanctions designations since 2009); U.S. DEP'T OF THE TREASURY, *THE TREASURY 2021 SANCTIONS REVIEW 2* (2021) (OFAC sanctions designations increased 933% since the year 2000).

² See *Sanctions Programs and Country Information*, OFF. OF FOREIGN ASSETS CONTROL, <https://ofac.treasury.gov/sanctions-programs-and-country-information> [https://perma.cc/DR5F-JTW4] (last visited Apr. 12, 2023).

³ Jonathan Masters, *What Are Economic Sanctions*, COUNCIL ON FOREIGN RELS. (Aug. 12, 2019), <https://www.cfr.org/background/what-are-economic-sanctions> [https://perma.cc/S2QR-9SUE]; CORY WELT ET AL., CONG. RSCH. SERV., R45415, *U.S. SANCTIONS ON RUSSIA* 41 (2022) (explaining that U.S. sanctions against Russia are "intended to be smart sanctions that target individuals and entities responsible for offending policies and/or associated with key Russian policymakers but inflict[] minimal collateral damage to the Russian people").

⁴ See, e.g., TRACEY DURNER & LIAT SHETRET, *UNDERSTANDING BANK DE-RISKING AND ITS EFFECT ON FINANCIAL INCLUSION* 3-4, 13 (2015).

⁵ See, e.g., Emmanuel Breen, *Corporations and US Economic Sanctions: The Dangers of Overcompliance*, in *RESEARCH HANDBOOK ON UNILATERAL AND EXTRATERRITORIAL SANCTIONS* 256, 258 (Charlotte Beaucillon ed., 2021).

finance lawful food, medicinal, or other transactions with a sanctioned entity or jurisdiction.⁶ At times, concerns with overcompliance have led observers to object to the U.S. sanctions program as structurally, strategically, and even morally flawed.⁷

This conversation has not been one-sided, however.⁸ Some have embraced overcompliance as a boon to U.S. sanctions policy—one that serves both to enhance their efficacy and prove their effectiveness.⁹ Contending that broad embargoes are more effective because they eliminate “ambiguity” and the space for “creative interpretation,”¹⁰ some have suggested that the explanations and guidance Treasury officials provide regarding sanctions enforcement in an effort to reduce overcompliance “are little more than roadmaps for sanctions violators to follow.”¹¹ In this telling, OFAC’s efforts to address overcompliance undermines U.S. sanctions policy rather than reinforcing it.

This Article takes a middle course. U.S. sanctions authorities are a critical component of the United States’ economic statecraft, and will rightfully remain so. As practitioners in this space, we know that participants in the global economy are wise to seek compliance with these authorities, not least because of the significant civil and criminal penalties that can attach for failure to comply,¹² as well as

⁶ See, e.g., Grégoire Mallard et al., *The Humanitarian Gap in the Global Sanctions Regime: Addressing Causes, Effects, and Solutions*, 26 GLOB. GOVERNANCE 121, 121 (2020).

⁷ See, e.g., Richard Hanania, *Ineffective, Immoral, Politically Convenient: America’s Overreliance on Economic Sanctions and What To Do About It*, CATO INST. (Feb. 18, 2020), <https://www.cato.org/policy-analysis/ineffective-immoral-politically-convenient-americas-overreliance-economic-sanctions> [<https://perma.cc/J4XA-T82L>]; AGATHE DEMARAIS, BACKFIRE: HOW SANCTIONS RESHAPE THE WORLD AGAINST U.S. INTERESTS 65 (2022).

⁸ For a relatively more sanguine perspective, see Pierre-Hugues Verdier, *Sanctions Overcompliance: What, Why, and Does It Matter?*, 48 N.C. J. INT’L L. 471 (2023).

⁹ John Bolton, *The US Needs a Sanctions Policy Revolution*, THE HILL (Dec. 1, 2022), <https://thehill.com/opinion/international/3757034-the-us-needs-a-sanctions-policy-revolution/> [<https://perma.cc/X8H7-MRX4>].

¹⁰ *Id.*

¹¹ *Id.*

¹² See *infra* Section III.A; see also, e.g., Press Release, U.S. Dep’t of Justice, BNP Paribas Sentenced for Conspiring to Violate the International Emergency Economic Powers Act and the Trading with the Enemy Act (May 1, 2015), <https://www.justice.gov/opa/pr/bnp-paribas-sentenced-conspiring-violate-international-emergency-economic-powers-act-and> [<https://perma.cc/A2LF-LDHB>].

the significant reputational harm¹³ that can come if the market even perceives potential non-compliance by a counterparty. But overcompliance also raises serious difficulties for U.S. national security policy. A calibrated U.S. sanctions policy requires Treasury officials to address overcompliance when and where they can—failure to do so threatens not only to turn “smart” sanctions “dumb” (reverting to the old-fashioned jurisdiction-wide restrictions) but to undermine the entire architecture upon which this important tool of statecraft rests. Overcompliance threatens to undermine U.S. sanctions as an effective tool in the United States’ economic statecraft toolkit in four ways: (1) by undermining the ability of U.S. policymakers to effectively calibrate sanctions so as to successfully extract desired behaviors on the part of target states; (2) by empowering the targeted state and other nefarious actors in the place of private and non-profit organizations, potentially driving corruption, extremism, and illicit financial transactions; (3) by imposing unnecessary humanitarian costs on civilian populations of the targeted state; and (4) by threatening the strength and logic of the U.S. dollar as the leading global reserve currency.

At their core, U.S. sanctions seek to coercively incentivize behavioral changes on the part of targeted entities through a bargaining model. They primarily function as coercive bargaining chips, at various times used both to deter and to punish actions viewed as contrary to U.S. foreign policy priorities and objectives. For instance, in 2021, the United States, along with the European Union and United Kingdom, made sanctions threats the center of their deterrence strategy as Russia massed troops for a further invasion of Ukraine.¹⁴ And after Russia launched a full-scale invasion in 2022, the United States and its partners imposed sweeping sanctions as a punitive measure designed to raise the cost of the invasion such that the Kremlin would relent.¹⁵

¹³ See *infra* Section III.A.; see also, e.g., MICHAEL B. GREENWALD, *THE FUTURE OF THE UNITED STATES DOLLAR: WEAPONIZING THE US FINANCIAL SYSTEM* 5 (2020) (noting the “reputational” costs of perceived sanctions avoidance, and attributing this to the fact that “[i]f one party facilitates sanctions evasion, there is the potential for all of that party’s business partners to unwittingly involve themselves in criminal activity”).

¹⁴ Alan Cullison & Michael R. Gordon, *Ukraine Wants Military Support To Deter Russia While the U.S. Weighs Response*, *WALL ST. J.* (Dec. 24, 2021), <https://www.wsj.com/articles/ukraine-wants-military-support-to-deter-russia-while-the-u-s-weighs-response-11640363279> [<https://perma.cc/87ZE-68QK>].

¹⁵ See, e.g., *Secretary Antony J. Blinken with Chuck Todd of NBC’s Meet the Press*,

As explored below, overcompliance can undermine the functioning of that bargaining process by distorting the ability of U.S. sanctions policymakers to effectively calibrate sanctions activity. This distortion can occur in three phases of the bargaining process. First, during the *imposition* phase, overcompliance can result in a rush of de-risking activity that far exceeds the scope of activity expected by policymakers. Second, during the *application* phase, when the parties test one another's will and develop potential compromise solutions, overcompliance may undermine confidence on the part of a target state that sanctions relief will be substantial enough to warrant the proposed policy modification. And third, during the *reward* phase, when policymakers seek to make good on a negotiated agreement, overcompliance may limit the ability of policymakers to comply with commitments, undermining the value of continued cooperation on the part of the targeted state and incentivizing a reversal in policy by both sides.

Beyond this bargaining framework, overcompliance can empower targeted entities and nefarious actors, and can cause non-targeted individuals and entities to resort to smuggling, a shadow financial system, or corruption in pursuit of goods and services incident to ordinary and everyday life. And, as addressed more fully below, overcompliance also threatens to undermine core U.S. foreign policy goals by limiting humanitarian aid that can reach targeted countries.

This Article proceeds in six parts. Part II begins with an outline of the legal structure of U.S. sanctions programs, including their propensity to rely on financial institutions as the implementation, interpretation, and enforcement arms of American foreign policy. Part III then highlights the incentives that private actors—who serve as both enforcers of sanctions and targets of coercive penalties for non-compliance—face to overcomply with U.S. sanctions requirements, often by taking excessively cautious actions in their dealings with counterparties, de-risking large segments of their operations, and prohibiting even lawful and beneficial commerce. In Part IV, we examine three case studies that highlight this dynamic

U.S. DEP'T OF STATE (Apr. 3, 2022), <https://www.state.gov/secretary-antony-j-blinken-with-chuck-todd-of-nbcs-meet-the-press-3/> [<https://perma.cc/W7HN-SAXL>] (“The purpose of the sanctions . . . is not to be there indefinitely. It’s to change Russia’s conduct. And if, as a result of negotiations, the sanctions, the pressure, the support for Ukraine, we achieve just that, then at some point the sanctions will go away.”).

in recent years, looking to examples from Russia, Iran, and Afghanistan. Part V addresses in detail the national security tradeoffs that arise from overcompliance, while Part VI proposes potential steps OFAC can take to mitigate the negative byproducts of sanctions overcompliance, pointing to actions such as OFAC's recent enactment of a humanitarian exemption applicable across all sanctions programs as an important first step. Part VII concludes.

II. The Structure of U.S. Sanctions Programs: Putting Private Actors on the Front Lines

Historically, U.S. sanctions took the form of broad, jurisdiction-wide embargoes.¹⁶ Beginning in the 1990s and accelerating following the attacks of September 11, 2001, however, the United States significantly overhauled its sanctions program, shifting away from comprehensive embargoes and instead focusing on “targeted” or “smart” sanctions.¹⁷ Today, U.S. persons are presumptively prohibited from engaging in substantially all transactions involving only a small number of jurisdictions, including Cuba, Iran, North Korea, Syria, and the Crimea, Donetsk People's Republic, and Luhansk People's Republic regions of Ukraine.¹⁸ At the same time, sanctions programs, authorities, and designations have multiplied exponentially.¹⁹

By and large, U.S. sanctions are “list-based”—that is, they prohibit U.S. persons from engaging in certain transactions with specified entities or persons, including any direct and indirect majority-owned entities.²⁰ Among other programs, the United States also imposes more limited restrictions in certain contexts. For example, the United States has imposed sectoral sanctions, a more recent innovation that prohibits U.S. persons from engaging in

¹⁶ William Reinsch, *Methinks Thou Dost Comply Too Much*, CTR. FOR STRATEGIC & INT'L STUD. (Jan. 11, 2023), <https://www.csis.org/analysis/methinks-thou-dost-comply-too-much> [https://perma.cc/95SV-Q4HK] (explaining that “[u]ntil the George W. Bush administration, sanctions tended to be generalized blanket affairs”).

¹⁷ Edoardo Saravalle, Note, *Recasting Sanctions and Anti-Money Laundering: From National Security to Unilateral Financial Regulation*, 2022 COLUM. BUS. L. REV. 550, 559-60 (2022).

¹⁸ 2022 *Year-End Sanctions and Export Controls Update*, GIBSON DUNN (Feb. 7, 2023), <https://www.gibsondunn.com/2022-year-end-sanctions-and-export-controls-update/> [https://perma.cc/YTT2-MQCP].

¹⁹ See Imperiale, *supra* note 1.

²⁰ *Id.*

certain types of activities with designated entities, as identified on the Sectoral Sanctions Identifications (“SSI”) List or the Non-SDN Menu-Based Sanctions (“NS-MBS”) List.²¹ Sectoral sanctions target a specific sector of an economy, and they “limit[] the types of interactions a targeted entity” within this sector is allowed to undertake with a U.S. person “pursuant to a series of OFAC ‘Directives.’”²² With respect to certain entities in the People’s Republic of China, for instance, the United States has imposed restrictions on investments in publicly traded securities of companies identified as a part of the Chinese military-industrial complex.²³

This shift away from embargoes and towards smart sanctions has had the effect of increasingly placing financial institutions on the frontline of Washington’s economic coercive statecraft, effectively outsourcing the conduct of U.S. foreign policy to private entities and utilizing banks and related institutions as the principal enforcers of U.S. sanctions.²⁴ At the same time, financial institutions are “targets of regulation and enforcement” themselves.²⁵ U.S. sanctions thus primarily operate by coercing business entities and investors that operate or have relationships with sanctioned

²¹ See *Sectoral Sanctions Identifications (SSI) List*, U.S. DEP’T OF THE TREASURY, <https://ofac.treasury.gov/consolidated-sanctions-list-non-sdn-lists/sectoral-sanctions-identifications-ssi-list> [<https://perma.cc/U8F5-SEQH>] (last updated Mar. 8, 2023); *Non-SDN Menu-Based Sanctions List (NS-MBS List)*, U.S. DEP’T OF THE TREASURY, <https://ofac.treasury.gov/consolidated-sanctions-list-non-sdn-lists/non-sdn-menu-based-sanctions-list-ns-mbs-list> [<https://perma.cc/655N-SPRA>] (last updated Feb. 24, 2023).

²² GIBSON DUNN, *supra* note 18.

²³ See *Non-SDN Chinese Military-Industrial Complex Companies List (NS-CMIC List)*, OFF. OF FOREIGN ASSETS CONTROL (Dec. 16, 2021), <https://ofac.treasury.gov/consolidated-sanctions-list/ns-cmic-list> [<https://perma.cc/TR39-6FWV>]; Exec. Order No. 14032, 3 C.F.R. § 14032 (2022).

²⁴ Saravalle, *supra* note 17, at 559; Daniel W. Drezner, *Targeted Sanctions in a World of Global Finance*, 41 INT’L INTERACTIONS 755, 756, 758 (2015) (noting increase in financial sanctions); Marco Fasciglione, *Unilateral and Extraterritorial Sanctions Symposium: Unilateral and Extraterritorial Sanctions—Economic Operators and the Rise of the Business and Human Rights International Legal Framework*, OPINIO JURIS (Feb. 3, 2022), <https://opiniojuris.org/2022/03/02/unilateral-and-extraterritorial-sanctions-symposium-unilateral-and-extraterritorial-sanctions-economic-operators-and-the-rise-of-the-business-and-human-rights-international-legal-framework/> [<https://perma.cc/4MSC-RXEM>] (explaining that sanctions “give rise to a sort of ‘burden shifting’ on private operators who are requested to comply with coercive measures so as not to incur” penalties).

²⁵ Saravalle, *supra* note 17, at 559-60.

countries to limit or proscribe certain transactions.²⁶

Multiple factors permitted this revolution in sanctions policy, but its primary catalyst was the continuation of U.S. dollar dominance in global finance.²⁷ This relationship between sanctions and U.S. dollar dominance deserves some unpacking. The U.S. dollar constitutes almost sixty percent of allocated foreign exchange reserves,²⁸ falls on one side of eighty-eight percent of foreign exchange trades,²⁹ and is the currency of choice for approximately half of international payments.³⁰ Access to U.S. dollars is thus a critical component of international trade, regardless of the parties or jurisdictions involved.

To settle transactions denominated in dollars, a financial institution generally needs access to the U.S. financial system, regardless of where the financial institution or the parties to the transaction are located.³¹ To gain this access, foreign institutions typically open what are called “correspondent accounts” with a U.S. bank. Correspondent accounts operate as “a bank account for [the] bank” itself, allowing it to keep deposits in a U.S. bank and convert payments from a foreign currency into U.S. dollars on behalf of foreign clients.³²

If banks are denied this access, they may simply cease to exist. U.S. Treasury officials are well-aware of this fact. As David Cohen,

²⁶ William Mauldin, *U.S. Treasury's Top Terrorism Cop: How Financial Tools Fight Foes*, WALL ST. J. (June 2, 2014), <https://www.wsj.com/articles/BL-WB-46085> [<https://perma.cc/6FZS-343M>].

²⁷ Daniel W. Drezner, *The United States of Sanctions*, FOREIGN AFFS. (Aug. 24, 2021), <https://www.foreignaffairs.com/articles/united-states/2021-08-24/united-states-sanctions> [<https://perma.cc/7A9E-J8MA>].

²⁸ REBECCA M. NELSON & MARTIN A. WEISS, CONG. RSCH. SERV., IF11707, THE U.S. DOLLAR AS THE WORLD'S DOMINANT CURRENCY (2022); *see also* Carla Norrlöf, *The Dollar Still Dominates*, FOREIGN AFFS. (Feb. 21, 2023), <https://www.foreignaffairs.com/united-states/dollar-still-dominates> [<https://perma.cc/BGG7-JEPK>] (noting that the dollar accounts for sixty percent of central bank reserves while the Euro constitutes twenty percent and the yen six percent).

²⁹ BANK FOR INT'L SETTLEMENTS, TRIENNIAL CENTRAL BANK SURVEY: FOREIGN EXCHANGE TURNOVER IN APRIL 2016 4 (2016).

³⁰ NELSON & WEISS, *supra* note 28.

³¹ *Id.*

³² Joshua P. Zoffer, *The Dollar and the United States' Exorbitant Power to Sanction*, 113 AM. J. INT'L L. UNBOUND 152, 153 (2019). For a detailed overview of correspondent banking, *see* RENA S. MILLER, CONG. RSCH. SERV., IF10873, OVERVIEW OF CORRESPONDENT BANKING AND “DE-RISKING” ISSUES (2022).

then Treasury Under Secretary for Terrorism and Financial Intelligence, explained:

For banks and businesses around the world, if they don't have access to the U.S. financial system, don't have access to the U.S. economy, it is a significant if not mortal wound. That gives us a huge amount of leverage, a huge amount of opportunity to project U.S. power through our financial measures.³³

The Treasury Department relies principally on three statutory authorities when constructing U.S. sanctions programs. Under both the Trading with the Enemy Act and the International Emergency Economic Powers Act, the Treasury operates the Specifically Designated Nationals (“SDN”) List—a list of entities and individuals with whom U.S. persons are banned from transacting.³⁴ Entities on the SDN list are in essence *persona non grata* to the U.S. financial system, and U.S. financial institutions are required to block their assets and prohibit their transactions.³⁵ These two authorities thus permit the United States to “freeze financial assets and prohibit or limit financial transactions,” as well as “impede trade by making it difficult to pay for the export or import of goods and services.”³⁶

Finally, Section 311 of the Patriot Act permits OFAC to force U.S. financial institutions to refuse services to any entity designated as a “primary money laundering concern.”³⁷ Because this same provision authorizes OFAC to bar U.S. banks from providing correspondent accounts to designated entities, the Treasury has utilized it to great effect, effectively banishing designated entities from global financial markets.³⁸ This tool has been used against

³³ *Id.*; Mauldin, *supra* note 26.

³⁴ 50 U.S.C. §§ 1701-1702, 4302-4343.

³⁵ See *What is an SDN?*, OFF. OF FOREIGN ASSETS CONTROL (Sept. 10, 2022), <https://ofac.treasury.gov/faqs/18> [<https://perma.cc/XUG8-3SEX>]; *Specially Designated Nationals and Blocked Persons List (SDN) Human Readable Lists*, OFF. OF FOREIGN ASSETS CONTROL, <https://home.treasury.gov/policy-issues/financial-sanctions/specially-designated-nationals-and-blocked-persons-list-sdn-human-readable-lists> [<https://perma.cc/2DDW-C9R9>] (last updated Apr. 12, 2023).

³⁶ Barry E. Carter & Ryan M. Farha, *Overview and Operation of U.S. Financial Sanctions, Including the Example of Iran*, 44 GEO. J. INT'L L. 903, 904 (2013).

³⁷ 31 U.S.C. § 5318A(b).

³⁸ Fasciglione, *supra* note 24 (highlighting the example of a Latvian bank, ABLV, that folded within a matter of days after Treasury designated it as a money laundering concern); Patricia Kowsmann, *ECB Pulls Plug on Latvia's Failing ABLV Bank*, WALL ST. J. (Feb. 24, 2018), <https://www.wsj.com/articles/ecb-pulls-plug-on-latvias-failing-ablv->

specific financial institutions, or even against entire countries, such as Iran.³⁹

U.S. sanctions derive their potency from the interconnectedness of the global financial system, and its reliance in turn on the architecture of U.S. dollar-denominated finance.⁴⁰ Because “such a large number of global transactions clear through the United States, a significant volume of worldwide financial transactions are subject to the US sanctions regime.”⁴¹ Even sanctioned actors themselves rely on the U.S. financial system in order to process international transactions.⁴² They must rely on banks to process transactions, which, in a highly connected and globalized supply chain, are usually denominated in U.S. dollars. At the same time, financial institutions face tremendous—indeed, overwhelming—pressure to cut ties with illicit actors. Banks not only face potential civil and criminal penalties for violating U.S. sanctions,⁴³ they too face the potential death sentence of being barred from the U.S. financial system.⁴⁴ As a result, banks will choose to not do business with a sanctioned entity, as the choice between access to the U.S. financial system (and through it to the global financial system) and servicing the single account of a sanctioned entity is an easy one.⁴⁵ Faced with this choice, even non-U.S. banks will block sanctioned entities from using their services, turning U.S. unilateral sanctions into “*de facto* secondary sanctions.”⁴⁶

bank-1519447308 [https://perma.cc/9G7P-WXK5] (detailing collapse of ABLV).

³⁹ Arshad Mohammed & David Lawder, *U.S. to Name Iran Area of “Money Laundering Concern,”* REUTERS (Nov. 21, 2011), <https://www.reuters.com/article/us-iran-usa-sanctions/u-s-to-name-iran-area-of-money-laundering-concern-idUSTRE7AH2K920111121> [https://perma.cc/QBP7-U6MG].

⁴⁰ Brent J. McIntosh, *Wielding the Tools of Economic Statecraft*, 12 J. NAT’L SEC. L. & POL’Y 101, 104 (2021); Mallard et al., *supra* note 6, at 130-31.

⁴¹ Zachary Goldman & Alina Lindblom, *The US Position and Practice with Regards to Unilateral and Extraterritorial Sanctions: Reimagining the US Sanctions Regime in a World of Advanced Technology*, in RESEARCH HANDBOOK ON UNILATERAL AND EXTRATERRITORIAL SANCTIONS 130, 132 (Charlotte Beaucillon ed., 2021).

⁴² JUAN C. ZARATE, *TREASURY’S WAR: THE UNLEASHING OF A NEW ERA OF FINANCIAL WARFARE* 114-15 (2013).

⁴³ *See infra* Section III.A; 31 C.F.R. § 501, app. A.

⁴⁴ ZARATE, *supra* note 42, at 7.

⁴⁵ Mallard et al., *supra* note 6, at 132 (explaining that banks, as “for-profit organizations,” must weigh the “risk of high US fines” against “the lower cost of losing an Iranian client”).

⁴⁶ Zoffer, *supra* note 32, at 155.

III. Incentives for Overcompliance: Why Private Actors Go Further than Required

Overcompliance with U.S. sanctions has in recent years arisen as a significant topic of discussion, but overcompliance itself is not a novel concept. Indeed, scholars have long grappled with the potential of uncertain legal rules to drive “overcompliance”—that is, conduct that goes beyond that required by law, typically in a socially undesirable manner.⁴⁷

In the context of U.S. sanctions, some have defined overcompliance broadly to include any instance in which “companies take more extensive actions than strictly necessary to avoid risking a possible sanctions violation and hefty fine.”⁴⁸ But overcompliance is best understood as occurring when “a financial institution seeks to avoid perceived regulatory risk by *indiscriminately* terminating, restricting, or denying services to broad classes of clients, without case-by-case analysis or consideration of mitigation options.”⁴⁹ Or as the United Nations has defined it, overcompliance is a form of “*excessive* avoidance of risk.”⁵⁰

As understood in this manner, overcompliance may take the form of

- “blocking all financial transactions with a sanctioned country, entity, or individual when some transactions are

⁴⁷ See John E. Calfee & Richard Craswell, *Some Effects of Uncertainty on Compliance with Legal Standards*, 70 VA. L. REV. 965, 965 (1984) (analyzing ways in which uncertainty incentivizes actors to “overcomply” or “undercomply” with legal requirements); Richard Craswell & John E. Calfee, *Deterrence and Uncertain Legal Standards*, 2 J.L. ECON. & ORG. 279, 280 (1986) (discussing the problem of optimal deterrence when the application of a rule or standard is uncertain).

⁴⁸ Tristan Kohl, *Unilateral and Extraterritorial Sanctions Symposium: Extraterritorial Sanctions—Overcompliance and Globalization*, OPINIO JURIS (Feb. 3, 2022), <https://opiniojuris.org/2022/03/02/unilateral-and-extraterritorial-sanctions-symposium-extraterritorial-sanctions-overcompliance-and-globalization/> [https://perma.cc/86LA-SSUU].

⁴⁹ Press Release, U.S. Dep’t of the Treasury, Remarks by Acting Under Secretary Adam Szubin at the ABA/ABA Money Laundering Enforcement Conference (Nov. 16, 2015) (emphasis added).

⁵⁰ *Guidance Note on Overcompliance with Unilateral Sanctions and Its Harmful Effects on Human Rights*, U.N. HUM. RTS. OFF. OF THE HIGH COMM’R (June 28, 2022) (emphasis added), <https://www.ohchr.org/en/special-procedures/sr-unilateral-coercive-measures/resources-unilateral-coercive-measures/guidance-note-overcompliance-unilateral-sanctions-and-its-harmful-effects-human-rights> [https://perma.cc/NLQ7-J6JG].

authorized,”

- “deter[ing] authorized transactions by requiring cumbersome, onerous documentation or certification, charging higher rates or fees, or imposing discouraging long delays,” or
- “freez[ing] assets that are not targeted by sanctions, or deny[ing] individuals the possibility to open or maintain bank accounts or to engage in transactions simply because they are nationals of a sanctioned country.”⁵¹

U.S. government officials have at times objected to complaints regarding de-risking and overcompliance when those terms are broadly defined, and not without good reason. As then-Treasury Under Secretary David Cohen said in 2015, de-risking is not a problem if it constitutes “the closing or restricting of an account because a financial institution, applying an appropriately designed risk-based analysis, determines that it cannot manage the risk of illicit activity associated with a particular client.”⁵² That is precisely what responsible risk managers should do.

But overcompliance can, at its most extreme, indiscriminately “cut[] operators off from potential value-creating economic activities that would in effect not be a violation of any . . . sanctions.”⁵³ Because U.S. sanctions are primarily implemented by the financial sector, they affect “players especially primed to respond to regulation.”⁵⁴ As a result, “the short-term outcome of any new sanction . . . rule is to structure financial institutions’ internal compliance processes and to shape the flows of international capital.”⁵⁵

Overcompliance then is driven primarily by five features of U.S. sanctions programs: (1) the cost of failing to comply; (2) the cost of achieving “optimal” compliance; (3) the structure of compliance as mandated by OFAC; (4) the failure of Treasury authorities to

⁵¹ *Id.*

⁵² Press Release, U.S. Dep’t of the Treasury, Remarks by Under Secretary David Cohen at the ABA/ABA Money Laundering Enforcement Conference (Nov. 10, 2014).

⁵³ Kohl, *supra* note 48.

⁵⁴ Saravalle, *supra* note 17, at 555; Nicholas R. Parrillo, *Federal Agency Guidance and the Power to Bind: An Empirical Study of Agencies and Industries*, 36 YALE J. ON REGUL. 165, 194 (2019) (“[B]anks consider it important to stay on the agencies’ good side, and sensitivity to guidance is an important part of that.”).

⁵⁵ Saravalle, *supra* note 17, at 555-56.

adequately address ambiguity and uncertainty; and (5) the significant reputational costs that can arise from dealing with entities perceived to be affiliated with or adjacent to targeted jurisdictions, entities, or individuals.

A. The Cost of Failing to Comply

The United States has powerful tools to incentivize private sector entities to comply with U.S. sanctions, and OFAC does not hesitate to use these tools to punish companies that fail to comply. As explained above, failure to comply with U.S. sanctions obligations can result in massive civil fines and even criminal exposure for both entities and individuals.⁵⁶ Because firms are expected to implement U.S. sanctions programs by complying with their restrictions or otherwise face significant penalties, firms have substantial incentives to ensure that their business activities remain on the safe side of U.S. sanctions enforcement.

The sentencing of BNP Paribas, S.A., a global financial institution headquartered in Paris, brought this point home to financial institutions across the world. In 2015, the bank was forced to forfeit over \$8.8 billion and pay a criminal fine of \$140 million for sanctions violations.⁵⁷ The bank had allegedly processed billions of dollars in transactions through the U.S. financial system on behalf of sanctioned Sudanese, Iranian, and Cuban entities.⁵⁸ The fine was the largest ever imposed in a U.S. criminal case,⁵⁹ but it was far from the only one imposed on non-U.S. banks for sanctions violations. U.S. authorities have also fined HSBC Bank N.V. (\$1.921 billion), Standard Chartered (\$667 million); Credit Suisse AG (\$536 million), and Barclays Bank PLC (\$298 million), among dozens of others.⁶⁰

These enforcement actions had a profound effect on compliance around the globe. Indeed, as a result of these actions, “U.S. and European financial institutions now almost universally try to fulfill their sanctions obligations.”⁶¹ This transformation has caused some

⁵⁶ See *supra* Section II.

⁵⁷ Press Release, U.S. Dep’t of Justice, *supra* note 12.

⁵⁸ *Id.*

⁵⁹ *Id.*

⁶⁰ David Restrepo Amariles & Matteo M. Winkler, *U.S. Economic Sanctions and the Corporate Compliance of Foreign Banks*, 51 INT’L LAW. 497, 513-12 (2018).

⁶¹ ELIZABETH ROSENBERG & JORDAN TAMA, STRENGTHENING THE ECONOMIC

observers to suggest an “Americanization of compliance” is underway in European and other non-U.S. banks.⁶²

Because banks rely on access to U.S. dollars and correspondent accounts to process global transactions, “even the implicit threat of being denied such access has made most banks in the world reluctant to work with sanctioned entities.”⁶³ This has arguably made targeted U.S. sanctions even more effective. Unlike trade embargoes, which incentivize sanctioned entities to engage in black-market trade,⁶⁴ banks are almost entirely reliant on access to the U.S. dollar and their correspondent account relationships.⁶⁵ By outsourcing U.S. sanctions enforcement to private financial institutions with significant incentive to remain on the good side of U.S. regulators, and implementing crippling punishments for failure to comply, U.S. targeted sanctions can all but “expel[] [sanctioned parties] from the global financial system.”⁶⁶ For this reason, “[c]ountries like Iran, Russia, and Venezuela have been particularly vulnerable to U.S. sanctions because, as oil exporters, their principal source of foreign exchange and revenue is denominated in dollars.”⁶⁷

Nonetheless, because the cost of failing to comply with U.S. sanctions is so high, financial institutions’ risk-reward ratio can skew heavily towards de-risking, leading them to cut off clients that present *any* indicia of risk.⁶⁸ For many financial institutions, the benefits of a particular transaction from a heavily sanctioned jurisdiction are not worth the risk that such a transaction presents to their balance sheets: the “amount of money the institution [can] earn [is] simply too small to justify” the risk it would take on to complete the transaction or otherwise service the customer.⁶⁹

ARSENAL: BOLSTERING THE DETERRENT AND SIGNALING EFFECT OF SANCTIONS (2019).

⁶² Amariles & Winkler, *supra* note 60, at 500.

⁶³ Drezner, *supra* note 27.

⁶⁴ *Id.*

⁶⁵ See Mallard et al., *supra* note 6, at 130-31.

⁶⁶ Drezner, *supra* note 27.

⁶⁷ Goldman & Lindblom, *supra* note 41, at 133.

⁶⁸ See Mallard et al., *supra* note 6, at 130. Indeed, following U.S. enforcement actions, “incriminated European banks completely left any business tied to high-risk jurisdictions.” *See id.*

⁶⁹ Reinsch, *supra* note 16; see SUE E. ECKERT ET AL., CHARITY & SEC. NETWORK, FINANCIAL ACCESS FOR U.S. NONPROFITS 14-15 (2017) (describing the “seismic shift” in compliance programs since 9/11 and noting that they now include “comprehensive

For instance, if OFAC imposes primary sanctions applying only to U.S. persons, non-U.S. financial institutions could proactively determine not to provide services to individuals or entities listed, even when they are permitted to do so (and U.S. policy may in fact *desire* that they do so).⁷⁰ On account of fear of OFAC penalties, “banks and other financial operators may refuse to transfer funds, or may require oft-onerous certification for each transfer, or create additional costs and delays that impede assistance.”⁷¹ These actions can “lead[] to difficulties in importing even basic food items, health-care equipment and other forms of humanitarian aid into sanctioned countries”—regardless of applicable humanitarian exemptions.⁷²

B. The Cost of “Optimal” Compliance

Somewhat paradoxically, financial institutions and other companies may also choose overcompliance as a cost-saving measure. As explained more fully below, U.S. authorities face tangible incentives to calibrate U.S. sanctions in a way that effectively deters and punishes targeted entities while permitting beneficial commerce that supports U.S. foreign policy goals. Private actors, however, do not share that same incentive structure—that is, they do not seek “optimal” compliance with U.S. sanctions. Instead, private actors seek to pursue profitable market transactions. To the extent that the value of a transaction or set of transactions is lower than the costs of ensuring those transactions comply with U.S. sanctions, private entities will often opt out of those transactions altogether.⁷³

Achieving “optimal” compliance in the context of a complex web of overlapping sanctions itself requires significant resources in time, human capital, and technology, all of which impose a substantial cost on companies operating internationally.⁷⁴ Some

management and reporting systems, transaction monitoring and . . . sanctions screening, enhanced procedures and controls for high-risk situations and a significant investment in resources”).

⁷⁰ Tom Ruys & Cedric Ryngaert, *Secondary Sanctions: A Weapon out of Control? The International Legality of, and European Responses to, US Secondary Sanctions*, BRIT. Y.B. INT'L L., 1, 16 (2020) (quoting a European bank’s compliance officer as saying that “[f]ear of sanctions even leads to over-compliance by non-US persons”).

⁷¹ Fasciglione, *supra* note 24.

⁷² *Id.*

⁷³ See DURNER & SHETRET, *supra* note 4, at 13.

⁷⁴ CAMERON JOHNSTON, E.U. INST. FOR SEC. STUD., SANCTIONS AGAINST RUSSIA:

reports have placed compliance costs for some financial institutions north of \$4 billion annually.⁷⁵ The larger and more complex a supply chain, or the more varied a customer base, the more difficult it will be for an entity to ensure compliance occurs from end to end.⁷⁶ Moreover, because entities can obscure their identities in an attempt to evade U.S. sanctions, compliance requires significant investments in know-your-customer evaluations and due diligence, not to mention tracking of ever-evolving U.S. designation lists and identified aliases.⁷⁷

Overcompliance thus can result when an entity determines that the benefits from a business opportunity in a sanctioned jurisdiction are outweighed by the costs of complying with the regulatory regime in place. In other words, some institutions simply “reject[] the role of primary watchdog in select markets and instead opt to remove themselves . . . altogether.”⁷⁸

C. *The Structure of Compliance*

Another factor that can drive overcompliance is the “risk-based analysis” structure of the modern compliance architecture. Violations of U.S. sanctions laws are a strict liability offense, but OFAC has considerable discretion and weighs a number of factors in determining whether to pursue an enforcement action against an entity.⁷⁹ These factors include “the actual or potential harm to sanctions programs caused” by the apparent violation, “economic benefit to the sanctioned entity,” the effect the apparent violation “had on the integrity of the U.S. sanction program,” license eligibility, whether the conduct constituted humanitarian activity, and the extent of cooperation with OFAC during the investigation.⁸⁰ Importantly, OFAC also weighs “the existence, nature, and adequacy” of any “risk-based OFAC compliance program at the

EVASION, COMPENSATION AND OVERCOMPLIANCE 4 (2015) (noting that compliance requires “[m]ultinational firms . . . to invest in the complex due diligence required to ensure that their . . . counterparts are not linked to sanctioned entities”).

⁷⁵ See ECKERT ET AL., *supra* note 69, at 23.

⁷⁶ Kohl, *supra* note 48.

⁷⁷ See Reinsch, *supra* note 16 (explaining the “cat and mouse game” financial institutions must play with sanctioned entities).

⁷⁸ DURNER & SHETRET, *supra* note 4, at 13.

⁷⁹ See 50 C.F.R. § 501, app. A.

⁸⁰ *Id.*

time of the apparent violation” as well as the “remedial response” pursued by the entity following the apparent violation.⁸¹

Evaluation of an entity’s risk-based compliance program at the enforcement stage encourages financial institutions to adopt a “broad safety buffer” to stay within regulatory expectations.⁸² That is, in order to expect leniency from OFAC for any potential slip ups or oversights, entities must first demonstrate that they have made a good-faith effort to account for and mitigate risks based on their customers’ locations and client rosters.⁸³ And because there is no “one-size-fits-all” framework, the precise contours of an adequate risk-based compliance program remain uncertain, encouraging entities to err on the side of risk aversion.

Beyond the risk-based approach itself, a comprehensive compliance program requires entities to take on the burden of enforcing U.S. sanctions. This means that entities must develop an apparatus for “freezing transactions, maintaining records and reporting high-risk transactions and suspicious activities, self-disclosures of cross-border movement of certain products . . . and financial accounts held in foreign jurisdictions.”⁸⁴ They are also responsible for the “collection and verification of information on customers and beneficial owners and sharing of information with other financial institutions, regulatory authorities, and law enforcement.”⁸⁵ Depending on the customer base and geographic location of a client roster, these operations will be more or less burdensome.

Finally, financial institutions previously subjected to U.S. government enforcement actions are likely to be particularly risk-averse as part of their ongoing remedial response.⁸⁶ For instance, following the United States’ entrance into the Joint Comprehensive Plan of Action (“JCPOA”) with Iran, some financial institutions that

⁸¹ *Id.*

⁸² ECKERT ET AL., *supra* note 69, at 12.

⁸³ OFF. OF FOREIGN ASSETS CONTROL, U.S. DEP’T OF THE TREASURY, A FRAMEWORK FOR OFAC COMPLIANCE COMMITMENTS (2019).

⁸⁴ ECKERT ET AL., *supra* note 69, at 15.

⁸⁵ *Id.*

⁸⁶ See generally Felicia Schwartz & Margot Patrick, *U.S. Secretary of State John Kerry Meets with European Bankers in Iran-Business Push*, WALL ST. J. (May 12, 2016), <https://www.wsj.com/articles/kerry-meets-with-european-bankers-in-iran-business-push-1463045793> [<https://perma.cc/QZ8J-83JH>].

had previously faced U.S. enforcement actions based on Iran sanctions violations refused to resume banking relationships in Iran.⁸⁷ Enforcement actions involving criminal settlement with the Department of Justice often end with a deferred prosecution agreement requiring financial institutions to bring on a sanctions compliance monitor.⁸⁸ These monitorships raise unique and ongoing challenges for financial entities, often requiring additional oversight, demonstrated improvement in technological screening processes and system enhancement, as well as extraordinary levels of remediation.⁸⁹ Even outside the context of criminal enforcement, OFAC has recently begun to require parties settling with the agency to agree to ongoing compliance commitments with the risk that OFAC will re-open a settled matter if those commitments are not met.⁹⁰ As a result, an entity that has already run afoul of U.S. sanctions law is likely to take extra steps to avoid the same outcome again.

D. Ambiguity and Uncertainty

Overcompliance is also driven by U.S. policy ambiguity and uncertainty regarding future sanctions activity. As in other contexts, U.S. sanctions “policy uncertainty has a sizeable detrimental effect

⁸⁷ *Id.* (reporting that Standard Chartered, Deutsche Bank, and HSBC refused to resume banking relationships with clients in Iran, pointing to deferred prosecution agreements with U.S. authorities); *see also, e.g., Standard Chartered Bank Admits to Illegally Processing Transactions in Violation of Iranian Sanctions and Agrees to Pay More than \$1 Billion*, U.S. DEP’T OF JUST. (Apr. 9, 2019), <https://www.justice.gov/opa/pr/standard-chartered-bank-admits-illegally-processing-transactions-violation-iranian-sanctions> [<https://perma.cc/3DVK-WF5P>].

⁸⁸ Ellen S. Zimiles et al., *Sanctions Monitorships*, in *THE GUIDE TO MONITORSHIPS* 1, 4-5 (3d ed. 2022) (detailing monitorships imposed on Standard Chartered Bank, HSBC, and Deutsche Bank, among others); Mallard et al., *supra* note 6, at 132 (pointing to monitorships in deferred prosecution agreements as driving heightened risk aversion among banks).

⁸⁹ *Id.* at 10-12.

⁹⁰ *See, e.g.,* OFF. OF FOREIGN ASSETS CONTROL, *supra* note 83, at 3; Off. of Foreign Assets Control, *Settlement Agreement with Standard Chartered Bank* 13-17 (2019), <https://ofac.treasury.gov/media/13921/download?inline> [<https://perma.cc/5T8V-29UK>]; Off. of Foreign Assets Control, *Settlement Agreement with UniCredit Bank Austria AG* 6-9 (2019), <https://ofac.treasury.gov/media/13926/download?inline> [<https://perma.cc/QTR8-C8LU>]; *see also* Jeremy Paner, *Compliance Certifications Jack Up Sanctions Violation Costs*, LAW360 (Apr. 30, 2019), <https://www.law360.com/articles/1154070/compliance-certifications-jack-up-sanctions-violation-costs> [<https://perma.cc/CH5N-V48C>].

on a firm's export investments and economic growth."⁹¹ And as the sanctions regime has multiplied in the number of programs and complexity, OFAC has at times struggled to keep up with the issuance of much-needed advice and guidance to the regulated community.⁹²

Ambiguity can be an asset, permitting OFAC maximum flexibility in ferreting out and pursuing sanctions violators while restricting their ability to game U.S. sanctions. But this ambiguity also undermines the effectiveness of U.S. general licenses (regulatory exemptions to sanctions) aimed to advance policy priorities beyond strictly limiting a sanctioned entity's access to financial markets. Even when OFAC issues a general license authorizing a particular type of transaction, private entities may struggle to understand its scope (and worry that it may be revoked), and therefore choose to err on the side of caution lest they face significant enforcement action.⁹³

Uncertainty as to future policy outcomes can also encourage overcompliance on the part of financial institutions and other entities. Private sector actors are often reticent to make significant investments in a targeted jurisdiction or sector out of fear that the United States could undertake a sanctions "U-turn" following the next election.⁹⁴ When relationships have been severed, contracts breached, and investments redirected for a significant period of time, restarting the flow of commerce can take significant resources, let alone will. Firms will naturally hesitate to invest resources into a jurisdiction that they view as riskier without credible commitments from the United States that sanctions will not be reapplied without reason or warning.

E. Reputational Costs

Finally, private sector actors may also overcomply with sanctions out of a fear that any business relationship with a

⁹¹ Kohl, *supra* note 48.

⁹² See Reinsch, *supra* note 16.

⁹³ See Karen Kramer, *Outdated U.S. Policies Are Helping Iran Censor Its Citizens*, FOREIGN POL'Y (May 6, 2021), <https://foreignpolicy.com/2021/05/06/iran-internet-censorship-us-sanctions/> [<https://perma.cc/F3KP-NDN7>] (explaining that even after OFAC issued a general license authorizing such transactions, technology firms refused to make products available in Iran because they lacked specific and detailed guidance as to what the general license authorized).

⁹⁴ Breen, *supra* note 5, at 264.

sanctioned country or entity could result in severe reputational consequences.⁹⁵ For instance, when pulling out of Russia, McDonald's explained to customers that it had concluded "continued ownership of the business in Russia [wa]s no longer tenable, nor [wa]s it consistent with McDonald's values."⁹⁶ When even sophisticated parties with massive compliance departments have difficulty understanding the scope of U.S. sanctions, consumers are highly unlikely to understand the nuanced sanctions regime against a sanctioned party. Moreover, there has been a marked rise in the role of activist shareholders and aggressive non-governmental organizations ("NGOs") imposing further reputational risks on companies that do not comply with broader desires associated with certain human rights and related goals—even if those goals far exceed that which is required by U.S. sanctions.⁹⁷

Further, U.S. authorities may not always speak with one voice with regards to their expectations in terms of sanctions compliance. For instance, OFAC and other parts of the U.S. government may encourage continued engagement with certain sectors of a sanctioned country, but other parts of the government, such as the U.S. Congress, may not agree. This was the case in September 2022 when members of Congress "excoriated" executives from JP Morgan Chase and Citibank for continuing to do business with Russian oil and gas firms, even though U.S. sanctions permitted those very transactions, and Treasury officials lobbied for their

⁹⁵ See Fasciglione, *supra* note 24 (explaining that "complying with unilateral and extraterritorial sanctions is increasingly perceived as involving reputational . . . risk").

⁹⁶ *McDonald's to Exit from Russia*, MCDONALD'S (May 16, 2022), <https://corporate.mcdonalds.com/corpmcd/our-stories/article/mcd-exit-russia.html> [<https://perma.cc/MM38-2CFA>] (last visited Apr. 8, 2023).

⁹⁷ See Jordan Wolman & Debra Kahn, *Shareholder Activists Make Inroads*, POLITICO (Jul. 28, 2022), <https://www.politico.com/newsletters/the-long-game/2022/07/28/shareholder-activists-make-inroads-00048445> [<https://perma.cc/L9UK-T9GF>] (detailing growth of activist investor resolutions focused on corporate political influence, human rights, and other initiatives); see also Simon Jessop & Benjamin Mallet, *Activist Clearway Urges TotalEnergies to Exit Russia or Face Vote*, REUTERS (Mar. 11, 2022), <https://www.reuters.com/business/sustainable-business/exclusive-activist-clearway-urges-totalenergies-exit-russia-or-face-vote-2022-03-11/> [<https://perma.cc/M52Z-HGJY>] (reporting that activist investors had written to the Board of TotalEnergies, a major French energy company, calling on it to exit its Russian operations because of the war in Ukraine or face a vote at the next shareholder meeting).

continued processing.⁹⁸ This split between authorities—and the fact that Congress has become increasingly aggressive in not only engaging the Executive branch and the private sector on sanctions issues but also in legislating its own sanctions measures⁹⁹—can be confusing, especially for foreign entities unfamiliar with the nuances of how U.S. sanctions authorities are promulgated.

IV. Case Studies in Overcompliance: Russia, Iran, and Afghanistan

Instances of overcompliance can be found in almost every sanctions program the United States administers, but three case studies usefully demonstrate the policy tradeoffs and national security ramifications of overcompliance. Below, we examine instances of overcompliance in Russia, Iran, and Afghanistan.

A. Russia

Following the Kremlin's 2022 invasion of Ukraine, "a coalition of more than 30 democracies—together accounting for more than half of global economic output—clamped severe restrictions on trade with Russia."¹⁰⁰ The United States had maintained sectoral sanctions against Russia for almost a decade, beginning with the Kremlin's initial incursions into Ukraine in 2014, targeting Russia's financial, energy, defense, and oil sectors.¹⁰¹ But in the days after Russia's incursion, the Biden Administration released a flurry of

⁹⁸ See *Western Officials Need Banks' Help to Keep Money Flowing to Russia*, THE ECONOMIST (Nov. 24, 2022), <https://www.economist.com/finance-and-economics/2022/11/24/western-officials-need-banks-help-to-keep-money-flowing-to-russia> [https://perma.cc/G7L7-37YU].

⁹⁹ See Jason Bartlett & Megan Ophel, *Sanctions by the Numbers: U.S. Secondary Sanctions*, CTR. FOR A NEW AM. SEC. (Aug. 26, 2021), <https://www.cnas.org/publications/reports/sanctions-by-the-numbers-u-s-secondary-sanctions> [https://perma.cc/A97L-ZG3X] (outlining the increasing number of sanctions statutes passed by Congress).

¹⁰⁰ GIBSON DUNN, *supra* note 18. A general overview of the current sanctions regimes targeting Russia can be found in Don S. De Amicis & David P. Stewart, *Sanctions on Steroids: The Ukraine-Russia-Related Sanctions*, 48 N.C. J. INT'L L. 379 (2023).

¹⁰¹ See Off. of Foreign Assets Control, Directive 1 (As Amended on September 29, 2017) Under Executive Order 13662; Off. of Foreign Assets Control, Directive 2 (As Amended on September 29, 2017) Under Executive Order 13662; Off. of Foreign Assets Control, Directive 3 Under Executive Order 13662 (Sept. 12, 2014); Off. of Foreign Assets Control, Directive 4 (As Amended on October 31, 2017) Under Executive Order 13662.

new sanctions, including four new sectoral sanctions directives targeting Russia's most significant economic institutions.¹⁰²

These new directives prohibited U.S. financial institutions from participating in the primary or secondary markets for “new” bonds issued by Russia's central bank,¹⁰³ targeted Russia's largest financial institutions, prohibited U.S. institutions from maintaining or opening correspondent accounts on behalf of Sberbank,¹⁰⁴ barred U.S. persons from dealing in “new” debt or “new” equity of thirteen major Russian state-owned enterprises and financial institutions,¹⁰⁵ and blocked transactions involving the Central Bank of the Russian Federation, the National Wealth Fund, and the Ministry of Finance.¹⁰⁶ The Treasury Department also maintained a steady drumbeat of Russian additions to its sanctions lists.¹⁰⁷ By March 2022, President Joe Biden signed three executive orders that barred U.S. persons from making a “new investment” in the Russian energy sector, and then in any other sector as determined by the Secretary of the Treasury.¹⁰⁸ In April, a third executive order prohibited “new investment” in all sectors of the Russian economy.¹⁰⁹

These sanctions quickly crippled parts of the Russian economy. In part because of the rapid rollout of U.S. and multilateral sanctions and in part because the severe nature of the sanctions signaled Washington's continued willingness to escalate, this time period saw extreme de-risking on the part of thousands of companies that sought to limit their exposure to the Russian market—even when

¹⁰² GIBSON DUNN, *supra* note 18.

¹⁰³ See Off. of Foreign Assets Control, Directive 1A Under Executive Order 14024 (Feb. 22, 2022).

¹⁰⁴ See Off. of Foreign Assets Control, Directive 2 Under Executive Order 14024 (Feb. 24, 2022).

¹⁰⁵ See Off. of Foreign Assets Control, Directive 3 Under Executive Order 14024 (Feb. 24, 2022).

¹⁰⁶ See Off. of Foreign Assets Control, Directive 4 Under Executive Order 14024 (Feb. 28, 2022).

¹⁰⁷ See *Fact Sheet: The United States Continues to Target Russian Oligarchs Enabling Putin's War of Choice*, WHITE HOUSE (Mar. 3, 2022), <https://www.whitehouse.gov/briefing-room/statements-releases/2022/03/03/fact-sheet-the-united-states-continues-to-target-russian-oligarchs-enabling-putins-war-of-choice/> [https://perma.cc/6LMB-ANJ2].

¹⁰⁸ See Exec. Order No. 14066, 87 Fed. Reg. 37625 (Mar. 8, 2022); Exec. Order No. 14068, 87 Fed. Reg. 14381 (2022).

¹⁰⁹ See Exec. Order No. 14071, 87 Fed. Reg. 20999 (2022).

regulations did not require them to do so.¹¹⁰ As one German bank official described it, “Our risk appetite . . . has been reduced to zero.”¹¹¹

Indeed, in the aftermath of these announcements, financial institutions and other companies fled Russia.¹¹² Apple withdrew “all product sales,” Paypal and Netflix “suspended operations,” and Google stopped “accepting customers in the country” while YouTube blocked “all channels linked to Russian state-run media.”¹¹³ Even some Chinese financial institutions withdrew services from Russia.¹¹⁴ In total, more than a thousand companies have ceased or curtailed their operations in Russia since the start of the 2022 invasion.¹¹⁵

Policymakers did not expect this form of intense “self-sanctioning,”¹¹⁶ and they were caught off-guard by the multiple challenges this rapid decoupling caused, including food insecurity, inflation, and even uninsurable grain exports.¹¹⁷ OFAC failed to

¹¹⁰ GIBSON DUNN, *supra* note 18.

¹¹¹ Patricia Kowsmann et al., *Sanction Carve-Outs for Energy Aren't Enough to Keep Money Flowing to Russia*, WALL ST. J. (Mar. 2, 2022), <https://www.wsj.com/articles/sanction-carve-outs-for-energy-arent-enough-to-keep-money-flowing-to-russia-11646252514> [<https://perma.cc/RC3H-NHTR>].

¹¹² See, e.g., *id.*; Sam Goldfarb, *U.S. Funding Markets Show Signs of Stability Despite Russia Sanctions*, WALL ST. J. (Mar. 4, 2022), <https://www.wsj.com/articles/u-s-funding-markets-show-signs-of-stability-despite-russia-sanctions-11646359036> [<https://perma.cc/2PV7-GKWZ>]; Nat Rubio-Licht et al., *The War in Ukraine Is Putting Tech—from Companies to Governments—to the Test*, PROTOCOL (Mar. 1, 2022), <https://www.protocol.com/policy/russia-ukraine-war-tech> [<https://perma.cc/3PG9-2G6A>] (providing a list of companies—from Disney to General Motors to the dating app Bumble—that halted operations in Russia).

¹¹³ Klon Kitchen, *Why National Security Is a Shared Burden Between the State and the Private Sector*, AM. ENTER. INST. (Mar. 17, 2022), <https://www.aei.org/op-eds/why-national-security-is-a-shared-burden-between-the-state-and-the-private-sector/> [<https://perma.cc/579H-MX77>].

¹¹⁴ See *G-7 Finance Ministers Seek To Isolate Russia, Raise Costs for Putin: Latest*, BLOOMBERG (Apr. 21, 2022), <https://www.bloomberg.com/news/articles/2022-04-20/ukraine-update-mariupol-in-jeopardy-china-stands-with-moscow> [<https://perma.cc/8R83-9XT3>] (“Russian banks under sanctions won’t be able to issue UnionPay cards because the Chinese payments provider is concerned about the risk of secondary sanctions.”).

¹¹⁵ See *Yale CELI List of Companies Leaving and Staying in Russia*, YALE SCH. OF MGMT., <https://www.yalerussianbusinessretreat.com/> [<https://perma.cc/28T3-REE5>] (last updated Apr. 8, 2023).

¹¹⁶ GIBSON DUNN, *supra* note 18.

¹¹⁷ See Daniel Flatley et al., “*Self-Sanctioning*” of Russia Sparks Worries About

issue any guidance as to what it considered a “new investment” until June 6, 2022, when it issued a set of FAQs detailing its interpretation of the term.¹¹⁸ Treasury officials eventually extended new general licenses, as they were forced to take at times awkward steps to reiterate that the U.S. government wanted certain businesses—particularly agriculture and shipping—to remain active in Russia despite the sanctions it had imposed, an acknowledgement of the challenges of sanctioning a globally connected and large economy.¹¹⁹ As of January 2023, Treasury officials continued to visit banks and other large corporations in an effort to ameliorate their compliance concerns and facilitate authorized Russian business transactions.¹²⁰

B. Iran

The United States has imposed sanctions against Iran since the Islamic revolution in 1979, and Iran remains one of the most sanctioned jurisdictions in the world, with numerous overlapping and complex regimes developing and falling away over time.¹²¹ This web of sanctions seeks to address numerous issues: Iran’s human rights records, financing of international terrorism, and pursuit of nuclear weapons.¹²² It is no surprise then that overcompliance with sanctions on Iran demonstrates both the humanitarian difficulties that can arise and the bargaining problems that overcompliance causes.

During the period prior to the JCPOA, a number of technology companies denied Iranian users access to their free digital

Ripple Effects, BLOOMBERG L. (June 14, 2022), <https://news.bloomberglaw.com/international-trade/self-sanctioning-of-russia-sparks-worries-about-ripple-effects> [<https://perma.cc/KN4G-FS4E>].

¹¹⁸ *Publication of New and Amended Russia-Related Frequently Asked Questions*, U.S. DEP’T OF THE TREASURY (June 6, 2022), https://home.treasury.gov/policy-issues/financial-sanctions/recent-actions/20220606_33 [<https://perma.cc/2D3K-7WXS>].

¹¹⁹ *Western Officials Need Banks’ Help to Keep Money Flowing to Russia*, *supra* note 98.

¹²⁰ Daniel Flatley, *Treasury Officials Warn Banks over Sanction Compliance Overkill*, BLOOMBERG L. (Jan. 6, 2023), <https://news.bloomberglaw.com/banking-law/treasury-officials-warn-banks-over-sanctions-compliance-overkill> [<https://perma.cc/4F5U-KQ5Y>].

¹²¹ KOLJA BROCKMAN & KEITH A. PREBLE, *MITIGATING HUMANITARIAN IMPACT IN A COMPLEX SANCTIONS ENVIRONMENT* 4 (2021).

¹²² *Id.*

services,¹²³ even though OFAC explicitly authorized such transactions under a general license.¹²⁴ Moreover, despite applicable humanitarian exemptions, overcompliance has repeatedly caused difficulties in ordinary Iranians acquiring humanitarian and medical goods.¹²⁵ For instance, after the United States withdrew from the JCPOA and reimposed its “maximum pressure” campaign, Mölnlycke, a Swedish medical company, paused exports to Iran out of concern regarding U.S. secondary sanctions.¹²⁶ As a result, children with a rare skin condition, epidermolysis bullosa (or “EB”), were unable to access bandages made by the company.¹²⁷

The Treasury Department has taken steps to encourage financial transactions for medical supplies, such as issuing a general license permitting humanitarian transactions involving the Central Bank of Iran¹²⁸ and creating a “Swiss channel” for processing humanitarian transactions in Iran.¹²⁹ Financial institutions nonetheless remain risk

¹²³ Ali Bangi, *The Impact of Sanctions Overcompliance on Iran*, IRAN CYBER DIALOGUE (Mar. 28, 2016), <https://asl19.org/en/icd/2016/blog/2016-03-28-impact-of-sanctions-overcompliance.html> [<https://perma.cc/3KVF-VX22>].

¹²⁴ Off. of Foreign Assets Control, Iran General License D-1: General License with Respect to Certain Services, Software, and Hardware Incident to Personal Communications 1 (Feb. 7, 2014), <https://ofac.treasury.gov/media/7991/download?inline> [<https://perma.cc/NZW9-MGZR>] (authorizing the “exportation or reexportation, directly or indirectly, from the United States or by a U.S. person, wherever located, to Iran of fee-based services incident to the exchange of personal communications over the Internet, such as instant messaging, chat, email, social networking, sharing of photos and movies, web browsing, and blogging”).

¹²⁵ *Maximum Pressure: US Economic Sanctions Harm Iranians’ Right to Health*, HUM. RTS. WATCH (Oct. 22, 2019), <https://www.hrw.org/report/2019/10/29/maximum-pressure/us-economic-sanctions-harm-iranians-right-health> [<https://perma.cc/CKW5-LSYV>] (detailing numerous instances of overcompliance wherein humanitarian institutions were unable to export into Iran medical devices and materials, including U.S. organizations with humanitarian licenses).

¹²⁶ Fasciglione, *supra* note 24.

¹²⁷ Press Release, Off. of the High Comm’r for Hum. Rts., Over-compliance with US Sanctions Harms Iranians’ Right to Health (Oct. 19, 2021), <https://www.ohchr.org/en/press-releases/2021/10/over-compliance-us-sanctions-harms-iranians-right-health> [<https://perma.cc/DCF7-5KWB>].

¹²⁸ Off. of Foreign Assets Control, Iran General License No. 8A: Authorizing Certain Humanitarian Trade Transactions Involving the Central Bank of Iran or the National Iranian Oil Company 1 (2020), [.treasury.gov/media/48841/download?inline](https://ofac.treasury.gov/media/48841/download?inline) [<https://perma.cc/WH6F-8N8T>].

¹²⁹ Ian Talley & Benoit Faucon, *U.S., Swiss Formally Open Humanitarian Trade Channel to Iran*, WALL ST. J. (Feb. 27, 2020), [.wsj.com/articles/u-s-swiss-formally-open-humanitarian-trade-channel-to-iran-11582846163](https://www.wsj.com/articles/u-s-swiss-formally-open-humanitarian-trade-channel-to-iran-11582846163) [<https://perma.cc/5V9H-VBDZ>].

averse when it comes to facilitating these transactions.¹³⁰ This is no doubt in part because the Iranian economy is dominated by the state, including aspects of the Iranian Revolutionary Guard Corps.¹³¹ But some of these efforts to encourage humanitarian assistance have placed significant administrative burdens on humanitarian organizations, requiring them to “capture information on the identity of Iranian customers, account balances for those individuals and entities involved in the transaction, the business relationships of those individuals, written commitments from Iranian distributors that such aid would not go to sanctioned individuals or entities in Iran, and a litany of other documentation.”¹³² These policies have had the effect of deterring the very humanitarian transactions that the United States has repeatedly identified as being in the interest of U.S. policy.¹³³

Overcompliance with Iran sanctions has also complicated negotiations with Iran over its nuclear program. As part of the JCPOA, the United States lifted secondary sanctions associated with Iran’s nuclear program, authorizing non-U.S. persons to engage in financial and banking-related transactions with Iranian entities and individuals without running afoul of U.S. sanctions.¹³⁴ Other sanctions, particularly those addressed to the activities of U.S. persons, continued to apply.¹³⁵ Because the sanctions architecture on Iran involved numerous statutes, in addition to executive orders, President Barack Obama was limited in how much longstanding relief he could provide without new legislation.¹³⁶ However,

¹³⁰ Jarrett Blanc, *Coercion in the Time of the Coronavirus*, CARNEGIE ENDOWMENT FOR INT’L PEACE (Apr. 8, 2020), .org/2020/04/08/coercion-in-time-of-coronavirus-pub-81495 [https://perma.cc/E5J3-PYEV].

¹³¹ Tyler Cullis & Amir Jandjani, *The Anatomy of Humanitarian Trade with Iran*, LAWFARE (May 14, 2019), .lawfareblog.com/anatomy-humanitarian-trade-iran [https://perma.cc/UH5G-8LTU].

¹³² Keith Preble, *Sanctions Reform Should Start with the Treasury Office Enforcing Them*, WAR ON THE ROCKS (Nov. 9, 2021), .com/2021/11/sanctions-reform-should-start-with-the-treasury-office-enforcing-them/ [https://perma.cc/VN4N-PZY8].

¹³³ JACOB B. KURTZER, DENIAL, DELAY, DIVERSION: TACKLING ACCESS CHALLENGES IN AN EVOLVING HUMANITARIAN LANDSCAPE 21 (2019).

¹³⁴ U.S. DEP’T OF THE TREASURY, GUIDANCE RELATING TO THE LIFTING OF CERTAIN U.S. SANCTIONS PURSUANT TO THE JOINT COMPREHENSIVE PLAN OF ACTION ON IMPLEMENTATION DAY (2016).

¹³⁵ *Id.*

¹³⁶ See Jack Goldsmith, *Why Congress Is Effectively Powerless to Stop the Iran Deal (and Why the Answer Is Not the Iran Review Act)*, LAWFARE (July 20, 2015),

Congress would not agree to permanently lift any of the congressionally imposed sanctions, forcing President Obama to issue waivers every 90 to 180 days to prevent secondary sanctions from reactivating.¹³⁷ This system created significant uncertainty in the global business community, which largely balked at reinvesting in Iran.¹³⁸

Without a rush of reinvestment, Iran complained that it did not receive the benefit of its bargain.¹³⁹ Following these complaints, the State Department, including then-U.S. Secretary of State John Kerry, attempted to “persuade major non-U.S. banks that doing Iran-related business [wa]s not only permitted following the relaxation of Iran sanctions, but [wa]s actually encouraged.”¹⁴⁰ Yet while the State Department actively lobbied banks to resume banking relations with Iranian entities, these requests often puzzled major bank compliance officers.¹⁴¹ Steven Levey, then the Chief Legal Officer of HSBC, took to the *Wall Street Journal* to note that, although the Administration may want foreign banks to do business with Iran, it offered “no assurances as to how such activity would be subsequently viewed by U.S. regulatory and law-enforcement authorities,” nor could it assure banks that Iran no longer posed financial-crime risks.¹⁴² “For this reason,” Mr. Levey announced, “HSBC has no intention of doing any new business involving

.lawfareblog.com/why-congress-effectively-powerless-stop-iran-deal-and-why-answer-not-iran-review-act [https://perma.cc/NQ78-UJUE]; DIANNE E. RENNACK, CONG. RSCH. SERV., R43311, IRAN: U.S. ECONOMIC SITUATIONS AND THE AUTHORITY TO LIFT RESTRICTIONS 5-6 (Nov. 21, 2019).

¹³⁷ Jamil N. Jaffer, *Elements of Its Own Demise: Key Flaws in the Obama Administration's Domestic Approach to the Iran Nuclear Agreement*, 51 CASE W. RESRV. J. INT'L L. 77, 83, 90-91 (2019).

¹³⁸ Khatereh Vatankhah, *How Sanctions Relief Became a Tool in Iran's Domestic Battles*, AL-MONITOR (Apr. 20, 2016), <https://www.al-monitor.com/originals/2016/04/iran-jcpoa-swift-sanctions-cbi-seif.html> [https://perma.cc/3YDK-C6KL].

¹³⁹ *Id.*

¹⁴⁰ Schwartz & Patrick, *supra* note 86; Stuart Levey, *Kerry's Peculiar Message About Iran for European Banks*, WALL ST. J. (May 12, 2016), <https://www.wsj.com/articles/kerrys-peculiar-message-about-iran-for-european-banks-14630933488> [https://perma.cc/YH6E-Q5AF] (noting the “odd position” in which the U.S. government actively encouraged European banks to establish relationships that were illegal for American banks to undertake).

¹⁴¹ Levey, *supra* note 140.

¹⁴² *Id.*

Iran.”¹⁴³ Ultimately, Iran received “a smaller economic boost” than it had anticipated.¹⁴⁴

C. Afghanistan

Following the Taliban’s takeover of Afghanistan in 2021, overcompliance significantly hampered the ability of aid organizations to ameliorate the suffering ordinary Afghans faced with the pullout of U.S. troops.¹⁴⁵ The United States had long sanctioned the Taliban, requiring that financial institutions “freeze any assets associated with the Taliban that c[a]me under U.S. jurisdiction, while also criminalizing almost any transaction with a U.S. nexus involving the Taliban.”¹⁴⁶ Because the Taliban itself was subject to U.S. sanctions, and the Taliban became the *de facto* government of Afghanistan overnight, financial institutions and aid organizations faced the difficult question of whether Afghanistan itself was a sanctioned territory.¹⁴⁷

This problem was exacerbated because, when the Taliban seized power, OFAC had never clarified exactly who or what constitutes “the Taliban.”¹⁴⁸ Nor was it clear whether a state controlled by a sanctioned entity was itself sanctioned.¹⁴⁹ Compliance teams had good reason to think that the Afghan government could be considered a sanctioned entity: as a general matter, the property in which a sanctioned party has a majority interest is also sanctioned, even if the sanctioned party’s control is indirect or partial.¹⁵⁰ Due to the fact that the Taliban controlled the Afghan state once again, it

¹⁴³ *Id.*

¹⁴⁴ ROSENBERG & TAMA, *supra* note 61.

¹⁴⁵ Thorsten J. Gorney, *The Impact of Over-Compliance with Sanctions*, SANCTIONS.IO ((Sept. 23, 2022), <https://www.sanctions.io/blog/the-impact-of-over-compliance-with-sanctions> [<https://perma.cc/2SSA-HAWV>]).

¹⁴⁶ Adam M. Smith, *The Humanitarian and Policy Challenges of U.S. Sanctions on the Taliban*, JUST SEC. (Aug. 23, 2021), <https://www.justsecurity.org/77957/the-humanitarian-and-policy-challenges-of-u-s-sanctions-on-the-taliban/> [<https://perma.cc/FJ9G-EVLD>]; *see also* *Afghanistan’s Future: Assessing the National Security, Humanitarian, and Economic Implications of the Taliban Takeover*, 117th Cong. 3 (2021) (statement of Adam M. Smith, Partner, Gibson, Dunn & Crutcher, LLP).

¹⁴⁷ Smith, *supra* note 146.

¹⁴⁸ *Id.*

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

stood to reason that it was equally subject to U.S. sanctions.¹⁵¹ It was no surprise then that financial institutions immediately began to treat Afghanistan itself as a sanctioned jurisdiction, prohibiting transactions necessary to the flow of foreign aid.¹⁵²

As the situation deteriorated, OFAC issued a series of guidance letters to financial institutions, including Western Union and MoneyGram, explaining that they could continue to process personal remittances to Afghan citizens.¹⁵³ The move was calculated to loosen the flow of relief into the Afghan economy, which neared total collapse after the United States and foreign allies froze \$9 billion in Afghan assets.¹⁵⁴ The Treasury Department also issued a series of new general licenses designed to make it easier for aid organizations to provide relief to Afghans, permitting transactions involving the Taliban so long as the money was used for basic humanitarian purposes.¹⁵⁵ OFAC also clarified that “[t]here [we]re no OFAC-administered sanctions that generally prohibit[ed] the export or reexport of goods or services to Afghanistan, moving or sending money into and out of Afghanistan, or activities in Afghanistan, provided that such transactions or activities d[id] not involve sanctioned individuals, entities, or property in which sanctioned individuals and entities ha[d] an interest.”¹⁵⁶

¹⁵¹ *Id.*

¹⁵² Smith, *supra* note 146.

¹⁵³ Andrea Shalal, *U.S. Allows Personal Remittances to Flow to Afghanistan*, REUTERS (Sept. 2, 2021), <https://www.reuters.com/world/us/us-treasury-allows-personal-remittances-flow-afghanistan-2021-09-02/> [<https://perma.cc/TR7Y-VMLH>].

¹⁵⁴ *Id.*

¹⁵⁵ *See, e.g.*, Off. of Foreign Assets Control, Afghanistan-Related General License No. 14: Authorizing Humanitarian Activities in Afghanistan (Sept. 24, 2021), <https://ofac.treasury.gov/media/912996/download?inline> [<https://perma.cc/5NRK-VDZQ>]; Off. of Foreign Assets Control, Afghanistan-Related General License No. 15: Transactions Related to the Exportation or Reexportation of Agricultural Commodities, Medicine, Medical Devices, Replacement Parts and Components, or Software Updates in Afghanistan (Sept. 24, 2021), <https://ofac.treasury.gov/media/913001/download?inline> [<https://perma.cc/Q7M7-3598>]; Press Release, U.S. Dep’t of the Treasury, Treasury Issues Additional General Licenses and Guidance in Support of Humanitarian Assistance and Other Support to Afghanistan (Dec. 22, 2021); Michael Crowley & Alan Rappeport, *As Humanitarian Disaster Looms, U.S. Opens Door for More Afghanistan Aid*, N.Y. TIMES (Dec. 22, 2021), <https://www.nytimes.com/2021/12/22/us/politics/afghanistan-sanctions-aid-taliban.html> [<https://perma.cc/C6CW-PXMH>].

¹⁵⁶ Press Release, U.S. Dep’t of the Treasury, Treasury Issues Additional General Licenses and Guidance in Support of Humanitarian Assistance and Other Support to Afghanistan (Dec. 22, 2021).

Later statements and FAQs reiterated this point, with OFAC rolling out additional guidance as the humanitarian conditions in Afghanistan worsened. In February 2022, OFAC issued another general license explicitly authorizing “activities necessary to sustain essential social services such as health and education, preserve essential community systems, and promote livelihoods and social cohesion,” and advising financial institutions that they “can facilitate the broad range of activities needed to mitigate further worsening of Afghanistan’s economic and humanitarian crisis.”¹⁵⁷ OFAC continued to issue renewed guidance throughout 2022.¹⁵⁸

V. How Overcompliance Threatens to Undermine U.S. National Security Priorities

Overcompliance threatens to undermine the ability of U.S. sanctions as an effective tool in the United States’ economic statecraft toolkit in four ways: (1) by creating bargaining problems and undermining the ability of U.S. policymakers to effectively calibrate sanctions so as to successfully extract desired behaviors on the part of target states; (2) by empowering the targeted state and other nefarious actors in the place of private and non-profit organizations, potentially driving corruption, extremism, and illicit financial transactions; (3) by imposing unnecessary and unmandated humanitarian costs on civilian populations of the targeted state; and (4) by threatening dollar dominance in the long term.

A. Bargaining Problems

Policymakers, politicians, and political scientists alike understand sanctions principally as a bargaining tool.¹⁵⁹ Sanctions,

¹⁵⁷ *Why Did the Department of the Treasury Issue Afghanistan-Related General License (GL) 20, “Authorizing Transactions Involving Afghanistan or Governing Institutions in Afghanistan”?*, OFF. OF FOREIGN ASSETS CONTROL (Feb. 25, 2022), <https://ofac.treasury.gov/faqs/991> [<https://perma.cc/7B62-YDXC>].

¹⁵⁸ *See, e.g., U.S. DEP’T OF THE TREASURY, FACT SHEET: PROVISION OF HUMANITARIAN ASSISTANCE TO AFGHANISTAN AND SUPPORT FOR THE AFGHAN PEOPLE (2022)*, <https://ofac.treasury.gov/media/922136/download?inline> [<https://perma.cc/NHH8-8BSF>].

¹⁵⁹ Navin A. Bapat & Bo Ram Kwon, *When Are Sanctions Effective? A Bargaining and Enforcement Framework*, 69 INT’L ORG. 131, 133 (2015) (noting that much of the academic literature “conceptualizes sanctions disputes as a bargaining problem” where each side “absorb[s] costs” until the target state relents, the sanctioning state abandons its demands, or the two reach a negotiated agreement); T. Clifton Morgan & Yoshiharu

as then-Treasury Secretary Jacob Lew argued, are designed to “create pressure to change future behavior.”¹⁶⁰ By “alter[ing] the incentives to which an adversary must respond,” sanctions “rais[e] the cost of . . . undesirable behavior.”¹⁶¹

Because “sanctions episodes are fundamentally bargaining scenarios between the parties,”¹⁶² U.S. policymakers must be able to accurately calibrate sanctions pressure during three phase of bargaining: the imposition phase, the application phase, and the relief phase. Unmitigated overcompliance threatens to undermine sanctions as a tool of economic statecraft at all three phases.

1. Imposition Phase

In order to maintain the effectiveness of U.S. sanctions, it is crucial that the United States has the ability to “[c]alibrate economic pressure in a way that leaves room to punish additional bad behavior and reward improved behavior.”¹⁶³ As Brent McIntosh, Under Secretary for International Affairs at the Treasury during the Trump Administration, has explained, “[l]eaving at least some room to dial up the pressure puts bad actors in a situation in which they feel economic pain but also understand that it could get worse”—a “prospect . . . which discourages further bad behavior.”¹⁶⁴

The “self-sanctioning” following the Kremlin’s 2022 invasion of Ukraine is an example of how overcompliance can undermine the ability of policymakers to calibrate sanctions during the imposition phase of sanctioning. The extreme de-risking that immediately followed the initial announcements of new sanctions was not part

Kobayashi, *Talking to the Hand: Bargaining, Strategic Interaction, and Economic Sanctions*, 134 EUR. ECON. REV. (VIRTUAL SPECIAL ISSUE) 1, 2 (2021) (“The dominant theoretical perspective guiding research on economic sanctions views sanctions as tools of bargaining.”); Daniel W. Drezner, *Bargaining, Enforcement, and Multilateral Sanctions: When Is Cooperation Counterproductive*, 54 INT’L ORG. 73, 79 (2000) (“[A] sanctions dispute represents a bargaining tactic between the primary sender and the target.”).

¹⁶⁰ U.S. Treasury Secretary Jacob J. Lew on the Evolution of Sanctions and Lessons for the Future, CARNEGIE ENDOWMENT FOR INT’L PEACE (Mar. 30, 2016), <https://carnegieendowment.org/2016/03/30/u.s.-treasury-secretary-jacob-j.-lew-on-evolution-of-sanctions-and-lessons-for-future-event-5191> [https://perma.cc/SY8Q-W4FZ].

¹⁶¹ Goldman & Lindblom, *supra* note 41, at 132-33.

¹⁶² MICHAEL CHAITKIN, NEGOTIATION AND STRATEGY: UNDERSTANDING SANCTIONS EFFECTIVENESS 4 (2010).

¹⁶³ McIntosh, *supra* note 40.

¹⁶⁴ *Id.*

of the coalition's well-designed and publicly articulated strategy.¹⁶⁵ In the face of a rapid onslaught of economic disengagement, the coalition was forced to take several steps to reassure international markets and to keep the flow of oil and agricultural products flowing.¹⁶⁶

Mass overcompliance was triggered by multiple factors, including reputational concerns on the part of multinational companies who sought to signal their opposition to the war, and the unique circumstances presented by Russian aggression in Europe.¹⁶⁷ But this de-risking was also driven by the perception that sanctions could continue to rapidly escalate, and the unpredictability that those measures posed for future business operations.¹⁶⁸ In essence, firms sought to get out ahead of the Treasury Department, limiting OFAC's ability to preserve punishment for the future. Importantly, of the thousand-plus companies that have altered their operations in Russia since the 2022 invasion, *none* was compelled to do so by law at the time it made its decision.¹⁶⁹

This form of overcompliance raises significant concerns for economic statecraft moving forward. If officials do not have the capability to calibrate economic pressure at the imposition phase, sanctions will become a much less effective tool. For one, sanctions will be less attractive to policymakers if, by imposing limited measures, they prompt significant economic turmoil in international markets. For another, sanctions will be a riskier option, less like a smart tool that can be used to apply surgically precise pressure and more like a full-scale embargo or economic war, with the resulting consequences of significant escalation and the need to consider the

¹⁶⁵ See e.g., GIBSON DUNN, *supra* note 18.

¹⁶⁶ See Flatley, *supra* note 120.

¹⁶⁷ Clara Hudson, *Reputational Concerns Mount as US Companies Reconsider Russia*, BLOOMBERG L. (June 15, 2022), <https://news.bloomberglaw.com/esg/reputational-concerns-mount-as-us-companies-reconsider-russia> [<https://perma.cc/PRF7-ACB5>].

¹⁶⁸ See Sanne Wass, *Sanctions Against Russia May Prompt Iran-style De-risking by Banks*, S&P GLOB. (Mar 3, 2022), <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/sanctions-against-russia-may-prompt-iran-style-de-risking-by-banks-69179675> [<https://perma.cc/G4FP-LSPE>].

¹⁶⁹ Jeffrey Sonnenfeld & Steven Tian, *Some of the Biggest Brands Are Leaving Russia. Others Just Can't Quit Putin. Here's a List.*, N.Y. TIMES (Apr. 7, 2022), <https://www.nytimes.com/interactive/2022/04/07/opinion/companies-ukraine-boycott.html> [<https://perma.cc/XL5R-EBRK>].

effects of such escalation.¹⁷⁰ And finally, sanctions may prove less effective if, in the long run, policymakers can no longer apply pressure while holding out the risk that “it could get worse.”¹⁷¹

2. *Application Phase*

Just as keeping the prospect of additional pressure in reserve strengthens the United States’ bargaining position, “the effectiveness of economic pressure often depends on bad actors’ believing that rectifying their behavior will benefit them.”¹⁷² If negotiators cannot credibly signal that they will be able to offer effective sanctions relief, targeted actors have little incentive to negotiate or otherwise change their behavior.¹⁷³

This form of overcompliance varies from that discussed in the relief phase, in that it threatens the bargaining process itself before OFAC has formally lifted sanctions. Instead, overcompliance during the application phrase casts doubt on the future ability of a sanctioner to effectively implement relief. This was a principal concern of Iranian negotiations in the lead up to the JCPOA, as Iran sought assurances that sanctions relief was more than an illusory promise.¹⁷⁴ This concern in part led the United States to include a clause in an annex to the JCPOA “commit[ting]” that the United States would permit the sale of commercial passenger aircraft to Iran.¹⁷⁵

¹⁷⁰ ADAM M. SMITH ET AL., U.S., EU, AND UN SANCTIONS: NAVIGATING THE DIVIDE FOR INTERNATIONAL BUSINESS 8 (2019).

¹⁷¹ McIntosh, *supra* note 40.

¹⁷² *Id.* at 105.

¹⁷³ ROSENBERG & TAMA, *supra* note 61 (explaining that bargaining credibility requires a counterparty to believe both that relief is possible and that the other party will grant that relief).

¹⁷⁴ Kelsey Davenport, *Sanctions Relief Timing Key to Iran Deal*, ARMS CONTROL ASSOC. (Mar. 2015), <https://www.armscontrol.org/act/2015-03/news/sanctions-relief-timing-key-iran-deal> [<https://perma.cc/AG7F-6Z59>]; *Negotiators Make Last Ditch Effort to Break Deadlock in Iran Talks*, TIMES OF ISR. (June 19, 2012), <https://www.timesofisrael.com/negotiators-trying-to-break-deadlock-with-iran/> [<https://perma.cc/5SA7-DVNZ>].

¹⁷⁵ Joint Comprehensive Plan of Action annex II, § 5.1, July 14, 2015, <https://2009-2017.state.gov/documents/organization/245320.pdf> [<https://perma.cc/7UYM-CHKD>]; Omar S. Bashir & Eric Lorber, *Boeing’s Art of the Iran Deal: How to Use Civilian Aircraft to Pressure the Regime*, FOREIGN AFFS. (Aug. 28, 2016), <https://www.foreignaffairs.com/print/node/1118204> [<https://perma.cc/4F5X-J4SM>].

3. *Relief Phase*

The inability to calibrate sanctions *relief* because of overcompliance also threatens to undermine U.S. national security policy priorities.¹⁷⁶ Once a sanctioned party has committed to a change in policy, it naturally expects something in return—principally, relief from sanctions. Failure to provide that relief can be grounds (valid or not) for the sanctioned party to return to its prior policy position, even garnering sympathy from parties that themselves previously supported or even imposed sanctions.¹⁷⁷ Thus, sanctioners must be able to “turn the spigot of ‘pain’ on *and* off against their targets,” otherwise sanctioned parties will come to believe that “sanctions are a permanent state of affairs.”¹⁷⁸ If that occurs, sanctions will be far less useful as a policy tool.¹⁷⁹

Unfortunately, as demonstrated following the JCPOA with Iran, sanctions overcompliance has in recent years hampered the ability of U.S. policy officials to deliver relief when desired.¹⁸⁰ Treasury officials can lift sanctions, but only private sector entities can turn the levers of commerce on again.¹⁸¹ Once sanctioned, a jurisdiction or entity retains a stigma, and institutions considering investments in the jurisdiction are likely to remain wary of the potential for U.S. policy U-turns.¹⁸²

¹⁷⁶ Drezner, *supra* note 27 (“The difficulty of removing sanctions from some countries complicates the United States’ efforts to bargain with all countries.”).

¹⁷⁷ ROSENBERG & TAMA, *supra* note 61 (explaining that when the lifting of sanctions does not afford economic relief, “countries have less of an incentive to make the political and legal concessions needed to have sanctions removed”).

¹⁷⁸ Richard Nephew, *The Hard Part: The Art of Sanctions Relief*, 41 WASH. Q. 63, 63 (2018).

¹⁷⁹ *Id.*

¹⁸⁰ See Suzanne Maloney, *Is the Iran Deal Unraveling? Think Again*, BROOKINGS INST. (May 20, 2016), <https://www.brookings.edu/blog/markaz/2016/05/20/is-the-iran-deal-unraveling-think-again/> [<https://perma.cc/5ZTQ-BD9Y>]; see Saeed Kamali Dehghan, *West Failing To Deliver Nuclear Deal Promises, Says Iran Vice-President*, THE GUARDIAN (Sept. 16, 2016), <https://www.theguardian.com/world/2016/sep/16/west-failing-deliver-nuclear-deal-promises-iran-vice-president-ali-akbar-salehi> [<https://perma.cc/8RKF-7R2U>].

¹⁸¹ ROSENBERG & TAMA, *supra* note 61 (noting that “the Obama administration could not compel the non-U.S. private sector to invest heavily in Iran and Cuba following the lifting of sanctions on them”).

¹⁸² Breen, *supra* note 5, at 264.

B. Empowerment of Targeted Actors and Other Nefarious Entities

Overcompliance can pose significant negative consequences for U.S. foreign policy objectives in two additional ways: first, overcompliance can empower the very people and entities U.S. policy seeks to punish by closing off alternative avenues of aid and support, and second, excessive compliance can push entities and individuals towards less transparent, more corrupt banking and trading systems.¹⁸³

For instance, in Iran, many companies continued to deny Iranians access to telecommunications and other technology services even after those services were no longer barred by U.S. sanctions and were instead perfectly legal.¹⁸⁴ This form of overcompliance threatened to undermine the growth of civil society in multiple ways. “In a society where access to online information is controlled by the authorities and publications are routinely subject to censorship,” overcompliance increased the barriers to access Iranians faced, undermining their ability to “bypass government controls on expression.”¹⁸⁵ And without access to verified versions of popular software, many Iranians instead purchased bootlegged versions that could be “designed to allow state authorities backdoor access to accounts.”¹⁸⁶ A lack of access to secure communications software “pose[d] grave security risks for users, who operate in a context where online content disapproved of by the state can land one in prison.”¹⁸⁷ As a result, “the very sanctions designed to provide political change in Iran” could, if not properly calibrated,

¹⁸³ Press Release, U.N. Hum. Rts. Off. of the High Comm’r, High Commissioner Calls for Critical Re-Evaluation of the Human Rights Impact of Unilateral Sanctions (Sept. 16, 2021) (“[T]hose sought to be targeted can in fact perversely benefit through gaming sanctions regime and profiteering from the economic distortions and incentives introduced by them.”); ECKERT ET AL., *supra* note 69, at 29 (de-risking can “create a vacuum [that is] filled by less transparent and accountable financial institutions”).

¹⁸⁴ Bangi, *supra* note 123; Kramer, *supra* note 93.

¹⁸⁵ Bangi, *supra* note 123.

¹⁸⁶ *Internet Freedom in Iran Will Benefit from Sanctions Relief*, CTR. FOR HUM. RIGHTS IN IRAN (Jan. 28, 2016), <https://iranhumanrights.org/2016/01/removal-of-sanctions-for-iranian-internet-users/> [<https://perma.cc/JZW3-7KT7>].

¹⁸⁷ Kramer, *supra* note 93.

“do just the opposite by disempowering Iranian citizens.”¹⁸⁸

In addition to empowering state actors while undermining the ability of ordinary citizens to voice dissent and organize effectively, technology overcompliance limits the ability of citizens to interact with the outside world. This last point—the loss of access to information from beyond the target state’s borders—also underscores the loss of American soft power that often comes with technology overcompliance. For instance, prior to the invasion of Ukraine, Instagram was Russia’s largest social media site, “with more than 80 million users, about 80 percent of whom followed Instagram accounts outside of their country.”¹⁸⁹ Without access to the platform, those users’ ability to gain information from individuals critical of the Russian invasion—and beyond the reach of President Vladimir Putin’s speech monitors—was significantly reduced.¹⁹⁰

Overcompliance also has the potential to close the legitimate channels of commerce, which can cause organizations and individuals to seek out other means to procure necessary goods, potentially fostering corruption, shadow financial networks, or other criminal activity.¹⁹¹ A system of overcompliance that pushes individuals and entities towards riskier channels of unregulated “underground banking” can actually increase the risk of untraceable funds making their way to illicit entities.¹⁹² Overcompliance also carries with it the potential to encourage violent extremism, as international programs designed to promote democracy, the rule of law, and civil rights are curtailed and individuals in desperate situations fall prey to radical ideologues.¹⁹³

¹⁸⁸ *See id.*

¹⁸⁹ Kitchen, *supra* note 113.

¹⁹⁰ *Id.* (noting that cutting off Instagram access “complicates efforts to get fact-based reporting and other critical information to Russian citizens”); Blanc, *supra* note 130.

¹⁹¹ Press Release, U.N. Hum. Rts. Council, Special Rapporteur on the Negative Impact of Unilateral Coercive Measures Says Guiding Principles Need to Be Drafted to Protect the Rights and Lives of People (Sept. 14, 2022), <https://www.ohchr.org/en/press-releases/2022/09/special-rapporteur-negative-impact-unilateral-coercive-measures-says-guiding> [<https://perma.cc/CYQ7-E7TA>]; *see also* STUART GORDON & SHERINE EL TARABOULSI-McCARTHY, COUNTER-TERRORISM, BANK DE-RISKING, AND HUMANITARIAN RESPONSE: A PATH FORWARD 4 (2018) (describing the risk of “black market” trading in food and fuel and the expansion of “networks of unregulated and potentially corrupt money brokers” in Yemen and Syria).

¹⁹² *See* ECKERT ET AL., *supra* note 69, at 29.

¹⁹³ *See id.* (drawing a connection between international aid programs and counter-

C. Humanitarian Harms

OFAC and numerous international organizations have consistently recognized the potential for sanctions overcompliance to undermine access to humanitarian goods and services. In its October 2021 review, the Treasury Department explained that while sanctions are an effective policy tool, they must be calibrated in order to address their potential impact on the flow of legitimate humanitarian aid to those in need.¹⁹⁴ And as the U.N. High Commissioner for Human Rights has recently explained, overcompliance at times makes it “difficult to import even basic food items, health-care equipment and other forms of humanitarian aid into sanctioned countries, despite the existence of applicable exemptions.”¹⁹⁵

Overcompliance affects the flow of humanitarian aid in some way in almost every country subject to U.S. sanctions,¹⁹⁶ but some instances are worse than others. In North Korea, for instance, “where humanitarian waivers are in place for some activities, banks’ overcompliance has led . . . to NGOs having to physically carry cash into the country to fund their work.”¹⁹⁷ Even the World Health Organization has encountered challenges transporting goods into countries under sanctions.¹⁹⁸

Humanitarian de-risking affects not only non-governmental actors and international organizations; it also threatens to undermine U.S.-authorized and taxpayer-funded aid. In one Government Accountability Office study, all nine USAID implementing partners reported instances in which banks closed their accounts, rejected transactions, or delayed processing over concerns related to U.S.

extremism); STAFF OF TASK FORCE TO INVESTIGATE TERRORISM FIN., 114TH CONG., 2D SESS., STOPPING TERROR FINANCE: SECURING THE U.S. FINANCIAL SECTOR 26 (2016) (“[A]s we work with U.S. and overseas financial institutions, let us not forget the laws of unintended consequences. If we so harshly regulate banks that they withdraw services from post-conflict and other developing countries that are ideal breeding grounds for terrorists and their financiers, we will drive the work of these financiers into the shadows . . .”).

¹⁹⁴ U.S. DEP’T OF THE TREASURY, *supra* note 1, at 5.

¹⁹⁵ Press Release, U.N. Hum. Rts. Off. of the High Comm’r, *supra* note 183.

¹⁹⁶ ROSENBERG & TAMA, *supra* note 61; ECKERT ET AL., *supra* note 69, at vii (describing overcompliance as a “serious and systemic challenge for the continued delivery of vital humanitarian and development assistance”).

¹⁹⁷ ANDREW BOYLE, CHECKING THE PRESIDENT’S SANCTIONS POWERS 16 (2021).

¹⁹⁸ *Id.*

sanctions.¹⁹⁹ When this occurs, NGOs are unable to pay employees, access spare parts required for medical equipment, or at times even book flights.²⁰⁰ Even when financial institutions agree that humanitarian activity is covered by a general license, they often determine the meager transaction amounts are not worth the added regulatory complexity required.²⁰¹

To be sure, there are legitimate reasons to control the end points of humanitarian aid. Government authorities have rightfully noted that it is vital that aid does not end up in the hands of sanctioned parties who could use it to extort others for political gain.²⁰² And even if “sanctioned entities use humanitarian assistance to benefit innocent populations,” that work “could allow the sanctioned entity to curry local support, undermining a goal of sanctions.”²⁰³ But the flow of humanitarian aid serves U.S. foreign policy in important ways, and its protection and facilitation should be prioritized—a process that requires attentive calibration and clear communication to ensure aid gets to vulnerable populations while not empowering sanctioned parties.

D. Threatening Dollar Dominance

Finally, overcompliance also threatens to undermine U.S.-dollar dominance—the very mechanism that makes U.S. sanctions devastatingly effective.²⁰⁴ Sanctions targets, and even more traditional allies of the United States, have already embarked on a process of displacing the dollar as the principal reserve currency.²⁰⁵

¹⁹⁹ U.S. GOV'T ACCOUNTABILITY OFF., GAO-21-239, VENEZUELA: ADDITIONAL TRACKING COULD AID TREASURY'S EFFORTS TO MITIGATE ANY ADVERSE IMPACTS U.S. SANCTIONS MIGHT HAVE ON HUMANITARIAN ASSISTANCE 28 (2021); *see also* U.S. GOV'T ACCOUNTABILITY OFF., GAO-18-669, HUMANITARIAN ASSISTANCE: USAID SHOULD IMPROVE INFORMATION COLLECTION AND COMMUNICATION TO HELP MITIGATE IMPLEMENTERS' BANKING CHALLENGES 2 (2018) (“Implementing [partners] for 7 of 18 Department of [State] and U.S. Agency for International Development (USAID) humanitarian assistance projects that GAO selected noted encountering banking access challenges.”).

²⁰⁰ Gorney, *supra* note 145.

²⁰¹ DURNER & SHETRET, *supra* note 4, at 13.

²⁰² BOYLE, *supra* note 197, at 16.

²⁰³ *Id.*

²⁰⁴ Drezner, *supra* note 27; *see also* Zoffer, *supra* note 32, at 152 (“The dollar’s special status as the world’s key currency affords the United States an unrivaled sanctioning power.”).

²⁰⁵ Drezner, *supra* note 27.

These efforts have so far proven unsuccessful, and there is reason to believe that displacing the U.S. dollar as the global reserve currency will be extraordinarily difficult.²⁰⁶ Nonetheless, despite its entrenched role in international commerce, the elasticity of the dollar's dominance is not infinite,²⁰⁷ and prudent policymakers will not accept the unnecessary costs to its credibility that come from overcompliance—a byproduct admittedly not in line with U.S. foreign policy goals.

Already, countries are pursuing digital currencies and other payment processes that could liberate them from the dollar's hegemonic role in global finance. China, for example, is experimenting with a digital yuan.²⁰⁸ But Beijing is not alone in this effort; according to the Congressional Research Service, ninety percent of central banks are at work creating digital currencies.²⁰⁹ And U.S. allies in Europe have constructed the Instrument in Support of Trade Exchanges (or "INSTEX"), a tool that would permit entities to trade with Iran by circumventing dollar-based transactions.²¹⁰ The European Union has also long made clear its objections in other ways, for example by putting in place Council Regulation 2271/96, a blocking statute that prohibited EU firms

²⁰⁶ Zoffer, *supra* note 32, at 152 ("The dollar's special status as the world's key currency affords the United States an unrivaled sanctioning power."); *see also* Joshua Zoffer, *Why the Dollar Doomsayers Have It Wrong*, FIN. TIMES (Nov. 27, 2019), <https://www.ft.com/content/127c77a4-007d-11ea-be59-e49b2a136b8d> [<https://perma.cc/Q49N-Y3TM>] (explaining that due to the dollar's role in international trade, payments, and banking, "governments alone cannot decide its fate"); Colin Weiss, *Geopolitics and the U.S. Dollar's Future as a Reserve Currency* 25 (Bd. of Governors of the Fed. Reserve Sys., Int'l Fin. Discussion Papers No. 1359, 2022) (concluding that "most government holdings of U.S. assets belong to those with close military ties to the U.S.," reducing the likelihood that they will shift away from the dollar).

²⁰⁷ Jonathan Wheatley & Colby Smith, *Russia Sanctions Threaten to Erode Dominance of US Dollar, Says IMF*, FIN. TIMES (Mar. 31, 2022), <https://www.ft.com/content/3e0760d4-8127-41db-9546-e62b6f8f5773> [<https://perma.cc/EGD4-HAMU>] (noting that dollar dominance is "unlikely to be challenged in the medium term," but explaining that some countries have begun renegotiating the currency in which transactions occur); *see also* CARLA NORRLÖF, WILL ECONOMIC STATECRAFT THREATEN WESTERN CURRENCY DOMINANCE?: SANCTIONS, GEOPOLITICS, AND THE GLOBAL MONETARY ORDER 4 (2022) (explaining that "[t]he sharpest decline in the dollar's reserve centrality coincides with the rise in the number of countries sanctioned by the US since 2017").

²⁰⁸ Drezner, *supra* note 27.

²⁰⁹ NELSON & WEISS, *supra* note 28.

²¹⁰ *Id.*; Preble, *supra* note 132.

from complying with U.S. secondary sanctions.²¹¹

At the end of the day, the dollar's exceptional role in international finance arises from voluntary choices—it is not mandated to continue. If utilizing U.S. dollars becomes too costly or restrictive for a sufficient number of entities, a competitor to the dollar could emerge, limiting U.S. sanctions power and crippling a critical U.S. foreign policy tool. Former Treasury Secretary Jack Lew explained sanctions' costs on the U.S. financial system:

While sanctions are a valuable alternative to more severe measures, including the lawful use of force, it is a mistake to think that they are low-cost. And if they make the business environment too complicated—or unpredictable, or if they excessively interfere with the flow of funds worldwide, financial transactions may begin to move outside of the United States entirely—which could threaten the central role of the U.S. financial system globally, not to mention the effectiveness of our sanctions in the future.²¹²

A competitor to the U.S. dollar is more likely to emerge if powerful foreign states perceive it as necessary to create alternatives to protect their interests from excessive U.S. sanctions.²¹³

VI. Addressing Overcompliance: Steps to Preserve a “Smart” Sanctions Policy

In recent years, OFAC itself has experimented with new methods of calibrating sanctions enforcement and ensuring that U.S. policy objectives are optimally advanced.²¹⁴ These efforts are to be commended. Yet, as the 2021 sanctions review acknowledged, there is also more that the Treasury could do to clarify sanctions policy, reduce harmful instances of overcompliance, and institutionalize processes that limit uncertainty and facilitate lawful transactions.²¹⁵ Below, we propose four suggestions for effectively calibrating U.S. sanctions policy in order to cabin the harm imposed by

²¹¹ Council Regulation 2271/96 of Nov. 22, 1996, Protecting Against the Effects of the Extra-Territorial Application of Legislation Adopted by a Third Country, and Actions Based Thereon or Resulting Therefrom, 1996 O.J. (L 309) 1, 2 (EC).

²¹² CARNEGIE ENDOWMENT FOR INT'L PEACE, *supra* note 160.

²¹³ Norrlöf, *supra* note 28 (arguing that the United States should seek to mitigate the “unintended effects” of sanctions so as to limit foreign states’ motivations to “find alternatives to the dollar”).

²¹⁴ See, e.g., *infra* notes 233-36.

²¹⁵ U.S. DEP'T OF THE TREASURY, *supra* note 1, at 4-7.

overcompliance.

A. Increased Clarity at the Time of Implementation

OFAC should endeavor to provide accompanying clarification, guidance, FAQs, and information detailing its rationale for sanctions *at the time of designation* to the greatest extent possible.²¹⁶ This is particularly important during the imposition phase, as a new sanctions program or designation has the potential to signal that additional sanctions may be forthcoming and thereby strengthen the enforcement signal OFAC sends beyond its intention. Moreover, more explicit guidelines detailing the steps a target must take to receive sanctions relief and the timelines and phasing of such relief would provide much-needed clarity to comfort risk-averse market participants weighing potential new investments.²¹⁷ To be sure, “concrete commitments regarding where the boundaries lie will sacrifice some amount of enforcement discretion.”²¹⁸ But “that loss should be weighed carefully against the nontrivial economic benefits of providing certainty to well-intentioned commercial actors.”²¹⁹ Moreover, Treasury should make clear what sort of actions need to be undertaken by designated actors in order for them to be considered for removal from the sanctions list. Such a process began under President Donald Trump’s Treasury Department with Secretary Steven Mnuchin regularly making clear how de-listing could occur at the time of announcing new sanctions.²²⁰ However,

²¹⁶ ROSENBERG & TAMA, *supra* note 61.

²¹⁷ Drezner, *supra* note 27 (explaining that “more explicit procedures for lifting sanctions would enhance the Treasury Department’s ability to reassure private-sector actors that once sanctions are lifted, they should feel safe doing business with the erstwhile targets”); *see also* JOHN BELLINGER ET AL., AMERICA’S USE OF COERCIVE ECONOMIC STATECRAFT 4 (2020) (emphasizing that “clear policy objectives are essential” and that clarity “enables policymakers to use coercive economic measures as effective diplomatic bargaining chips”).

²¹⁸ McIntosh, *supra* note 40.

²¹⁹ *Id.*

²²⁰ *See e.g.*, Press Release, U.S. Dep’t of the Treasury, Treasury Sanctions Venezuela’s State-Owned Oil Company Petroleos de Venezuela, S.A. (Jan. 28, 2019) (stating that “[t]he path to sanctions relief for PdVSA is through the expeditious transfer of control to the Interim President or a subsequent, democratically elected government”); Press Release, U.S. Dep’t of the Treasury, Treasury Sanctions Central Bank of Venezuela and Director of the Central Bank of Venezuela (Apr. 17, 2019) (explaining that “sanctions need not be permanent” and that the U.S. would remove sanctions against designated persons “who take concrete and meaningful actions to restore democratic order, refuse to take part in human rights abuses, speak out against abuses committed by the illegitimate

this process was never formalized, and although the Biden Administration has continued it intermittently, OFAC could strengthen U.S. sanctions programs by officially integrating de-listing criteria into the designation process.

B. Road Shows

OFAC has historically used “road shows” to emphasize to private entities, and in particular financial institutions, the risks of executing transactions in heavily sanctioned jurisdictions.²²¹ The lead author of this Article led several such road shows when he was at the Treasury Department. These meetings aim to explain why the Treasury has implemented sanctions on certain parties, and offer clarity to those on the front lines of sanctions enforcement as to the risks of certain types of transactions.²²² These road shows are important for generating compliance, but OFAC should also make a point of using them to encourage beneficial transactions that U.S. law does not bar.

In limited instances where OFAC has utilized road shows for this purpose, they appear to have been effective. For instance, following a bumpy start in which firms were left without guidance for months as to the scope of Russian sanctions, the Treasury Department eventually met with compliance teams and provided specific guidance as to which industries and what transactions were authorized.²²³ These efforts appear to have been successful in certain sectors, with wheat exports approaching normal levels and food prices dropping to a nine-month low as of November 2022.²²⁴

In the right circumstances, these in-person efforts to affirmatively encourage certain transactions could placate the concerns of compliance departments by clarifying OFAC’s policy objectives and enforcement priorities. Institutionalizing outreach may also break down barriers between enforcement authorities and

Maduro regime, and combat corruption in Venezuela”).

²²¹ Blanc, *supra* note 130.

²²² Daniel Flatley, *Treasury Officials Warn Banks over Sanctions Compliance Overkill*, BLOOMBERG L. (Jan. 6, 2023), <https://news.bloomberglaw.com/banking-law/treasury-officials-warn-banks-over-sanctions-compliance-overkill> [<https://perma.cc/7Y3U-ZRXX>].

²²³ *Western Officials Need Banks’ Help to Keep Money Flowing to Russia*, *supra* note 98.

²²⁴ *Id.*

regulated entities, freeing up channels of communication necessary to effectively calibrate sanctions activity in short order.

C. Comfort Letters

So-called “comfort letters,” which assure private sector entities that certain transactions are lawful and that U.S. authorities will not go after them if things go awry, can also play an important role in calibrating the effect of U.S. sanctions.²²⁵ OFAC has historically chafed at issuing formal assurances, but there is no statutory restriction on the agency doing so.²²⁶ These measures, particularly when used in crisis situations, can provide more tangible assurance than general licenses or guidance documents can yield, facilitating humanitarian and other beneficial transactions in service of U.S. policy interests. Moreover, if there is a single request of all parties seeking to comply with OFAC regulations, it is for the issuance of more comfort letters such that they can manage the actual and perceived risks of engaging in transactions in accordance with U.S. policy interests.

D. Humanitarian Exceptions

OFAC has long provided exceptions for humanitarian aid in the form of “general licenses,” which apply to anyone wishing to undertake specific humanitarian-related activities, and “specific licenses,” which approve applicants on a case-by-case basis to undertake a specific activity based on an application to OFAC to engage in otherwise prohibited transactions.²²⁷ But as OFAC recognized in its 2021 sanctions review (and as the case studies above illustrate, *see supra* Part IV), there exists space for the Treasury to, where appropriate, “expand sanctions exceptions to support the flow of legitimate humanitarian goods and assistance.”²²⁸ The Treasury Department can also do more to “provide clear guidance at the outset when sanctions authorities are created and implemented.”²²⁹ And OFAC should enhance its responsiveness to humanitarian crises as they unfold. For instance,

²²⁵ Blanc, *supra* note 130.

²²⁶ Smith, *supra* note 146.

²²⁷ See *What is a License?*, OFF. OF FOREIGN ASSETS CONTROL (June 16, 2016), <https://ofac.treasury.gov/faqs/74> [<https://perma.cc/D4NL-U6G2>].

²²⁸ U.S. DEP'T OF THE TREASURY, *supra* note 1, at 5.

²²⁹ *Id.*

although OFAC eventually issued general licenses for COVID-related activities,²³⁰ it waited a full fifteen months after the World Health Organization had declared a global pandemic to do so.²³¹ OFAC proved much more nimble in the wake of the Syria/Turkey earthquake in early 2023—it issued a general license to cover certain earthquake-related relief that involved the sanctioned government of Syria within three days of the quake.²³²

Recent steps by the Treasury following the United Nations Security Council’s adoption of Resolution 2664²³³ hold promise of further clarifying the scope of these humanitarian exceptions, as OFAC issued new or amended general licenses across all U.S. sanctions programs “to ease the delivery of humanitarian aid and ensure a baseline of authorizations for the provision of humanitarian support across many sanctions programs.”²³⁴ These guidelines, issued on December 20, 2022, provide authorizations in four categories, including the official business of the U.S. government, the official business of certain international organizations and entities, certain humanitarian transactions in support of NGOs’ activities, and the “provision of agricultural commodities, medicine, and medical devices, as well as replacement parts . . . for medical devices.”²³⁵ The NGO guidelines authorize nonprofits to engage in transactions with blocked entities and individuals if they are

²³⁰ Press Release, U.S. Dep’t of the Treasury, Treasury Issues Additional COVID-19-Related Sanctions Authorizations and Guidance (June 17, 2021).

²³¹ Domenico Cucinotta & Maurizio Vanelli, *WHO Declares COVID-19 a Pandemic*, 91 ACTA BIOMEDICA 157, 157 (2020).

²³² Off. of Foreign Assets Control, Syria General License No. 23: Authorizing Transactions Related to Earthquake Relief Efforts in Syria (Feb. 9, 2023), <https://ofac.treasury.gov/media/931106/download?inline> [<https://perma.cc/7XFJ-3ABN>]; see also Mengqi Sun, *U.S. Exempts Earthquake Aid to Syria from Sanctions*, WALL ST. J. (Feb. 10, 2023), <https://www.wsj.com/articles/u-s-exempts-earthquake-aid-to-syria-from-sanctions-918a78d0> [<https://perma.cc/ZU4H-ZAYL>]; Jared Malsin, *Turkey Earthquakes, a Timeline*, WALL ST. J. (Feb. 6, 2023), <https://www.wsj.com/livecoverage/turkeyearthquake/card/turkey-earthquakes-timeline-FRtiiz0eNX1jWs24p8rA> [<https://perma.cc/HA7K-BNV4>].

²³³ See generally S.C. Res. 2664 (Dec. 9, 2022).

²³⁴ Press Release, U.S. Dep’t of the Treasury, Treasury Implements Historic Humanitarian Sanctions Exceptions (Dec. 20, 2022).

²³⁵ *Id.*; *Are Financial Institutions Permitted to Provide Banking Services [Related to Activities Authorized Under the Four Categories of the General Licenses]? What Are OFAC’s Diligence Expectations . . . ?*, OFF. OF FOREIGN ASSETS CONTROL (Dec. 20, 2022), <https://ofac.treasury.gov/faqs/1106> [<https://perma.cc/7ZS9-2HWH>].

“designed to directly benefit the civilian population” and are “ordinarily incident and necessary” to activities in support of humanitarian projects to meet basic human needs, including disaster relief, food nutrition, or medicine distribution, as well as activities that support democracy building, the rule of law, access to information, education, sanitation, and environmental and natural resource protection.²³⁶ It will take time, however, to determine whether these new general licenses result in a meaningful reduction in overcompliance. After all, NGOs may find comfort in these exemptions, but the licenses need to change the calculations of financial institutions and other intermediaries (including insurers, freight forwarders, and others) in order to truly effectuate change on the ground.

VII. Conclusion

The current architecture of U.S. sanctions policy, built on the foundations of U.S. dollar dominance, effectively outsources the enforcement arm of U.S. foreign policy to the private sector. As a result, U.S. policy is at times less precise, less calibrated, and less responsive to rapidly evolving policy needs. This outsourcing can also result in private actors overshooting the mark in ways that are ultimately harmful to U.S. policy goals.

OFAC’s 2021 sanctions review rightfully recommended taking new steps to “calibrat[e] sanctions to mitigate unintended economic, political, and humanitarian impact.”²³⁷ These steps should include renewed and expanded efforts to clarify the scope of U.S. sanctions prohibitions, road shows to integrate and connect with the private sector, an uptick in comfort letters, and expanded humanitarian exceptions. If the discretionary judgments inherent in the enforcement of U.S. sanctions policy are outsourced to the private sector, Treasury officials must coordinate more closely with those sectors in order to optimally effectuate U.S. policy objectives and overcome the private sector’s understandable penchant for overcompliance.

²³⁶ 31 C.F.R §§ 536.514, 539.506 (2022).

²³⁷ U.S. DEP’T OF THE TREASURY, *supra* note 1, at 4.