The Department of the Treasury

Ensuring Prosperity *and* Security

ATMs with no cash. Resource-rich governments unable to pay soldiers' salaries. Debilitating unemployment and inflation. A decade ago, most U.S. military leaders were unconcerned about solving these issues. Far outside the military's core competencies, these were someone else's problem. Today, experience has taught us the complex and potentially caustic nexus of the security and economic realms. We now ignore these matters at our own peril.

The Department of Defense (DOD) is not alone in dealing with these concerns. The Department of the Treasury is an underleveraged, poorly understood interagency partner, specializing in macroeconomic and financial matters. An interagency featherweight—800 people are in its headquarters building—Treasury punches far above its weight class. However, heavyweights have inherent advantages in some fights. As a result, the better DOD can understand and work with this national security partner, the greater will be the Nation's prosperity and security.

Who Is Treasury?

The Treasury Department is the executive agency responsible for promoting America's economic prosperity and ensuring its financial security.[1] As anyone watching the news knows, this mission demands coordination with other economic and financial regulators, policymakers, and Wall Street entrepreneurs throughout the United States and abroad. Treasury also serves as the President's chief advisor on domestic and global economic and financial issues. This includes matters involving sustainable development, improved governance, stability of the global economy and financial system, and preventing the U.S. financial system from being used to fund illicit activity.

The Department has two primary components. First, Treasury's equivalent of the Pentagon, its Departmental Offices, resides next door to the White House. Defense personnel will most likely deal with professionals from this headquarters. Second, Treasury is responsible for its operating bureaus: the Internal Revenue Service, Mint, Bureau of Engraving and Printing, Financial Crimes Enforcement Network, Alcohol and Tobacco Tax and Trade Bureau, Bureau of Public Debt, Community Development Financial

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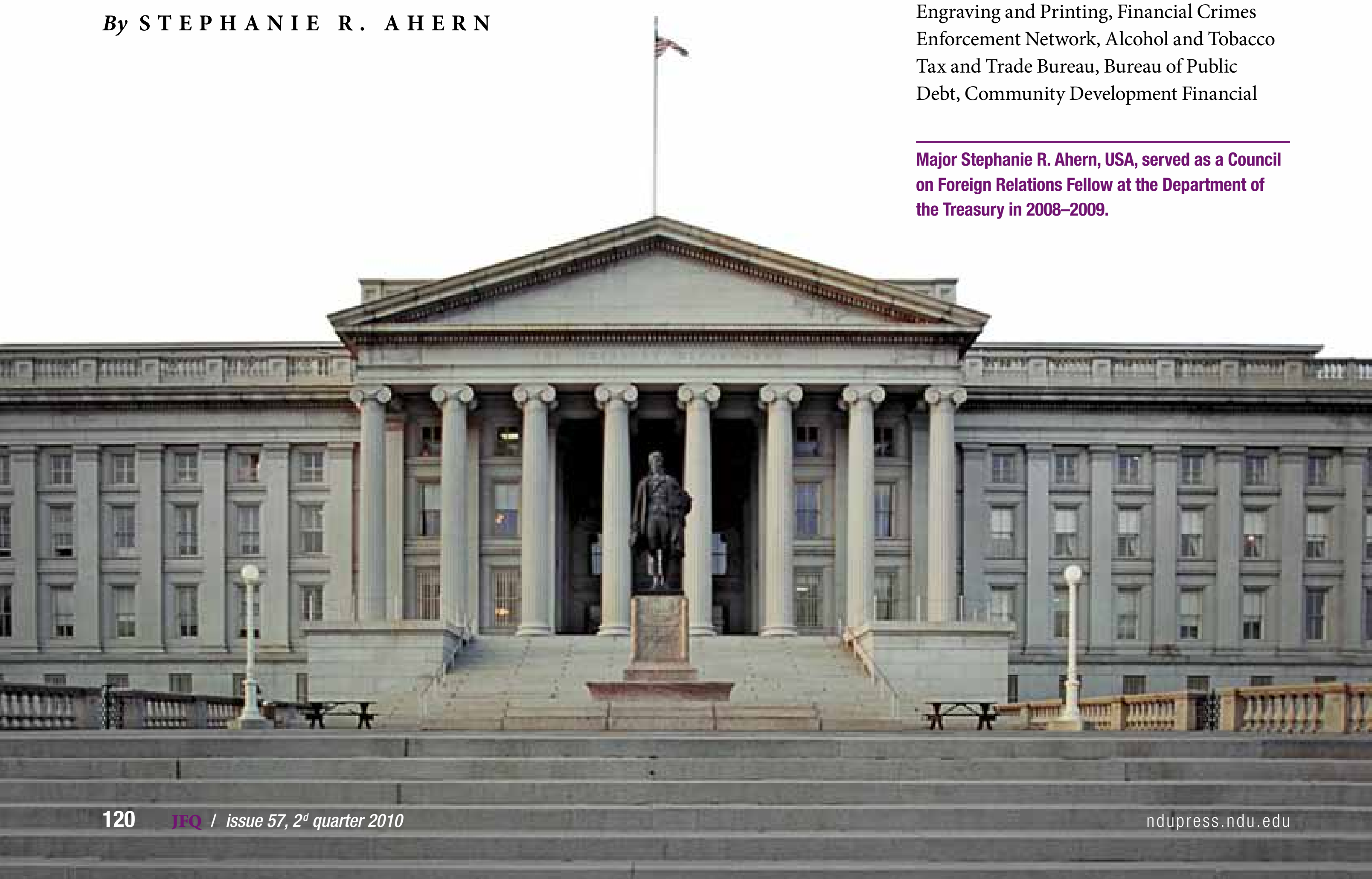

Institution Fund, Financial Management Service, Inspector General, Treasury Inspector General for Tax Administration, Office of the Comptroller of the Currency, and Office of Thrift Supervision. In total, the bureaus employ 98 percent of all Treasury employees.[2]

Long gone are the headquarters' money-laden vaults and frantic bank tellers. Instead, the headquarters houses the equivalent of three military "Services"—Domestic Finance, International Affairs, and Terrorism and Financial Intelligence—albeit at a fraction of the military Services' size. First, the Office of Domestic Finance deals with U.S.-based finance and banking matters, which are at the center of the current financial matters we see on the nightly news. It helps develop policies and guidance on financial institutions, financial market oversight and regulation, Federal credit policies, debt management, and state and local finance. It also oversees programs such as the deterrence of U.S. currency counterfeits and the Terrorism Risk Insurance Program. Most prominently, the office develops and coordinates Treasury's policies on legislative and regulatory issues affecting financial stability, including the Troubled Assets Relief Program (TARP).

Second, the Office of International Affairs (IA) specializes in macroeconomic matters worldwide. Its mission is to support and protect prosperity at home by encouraging financial stability and sound economic policies overseas. This office helps develop policies related to international economic, financial, monetary, trade, investment, debt, development, environment, bilateral aid, and energy programs. IA serves as the U.S. representative at the International Monetary Fund (IMF), World Bank, and other multilateral development banks. It also serves as the interagency chair of the Committee on Foreign Investment in the United States (CFIUS) process, reviewing potential sales of U.S. businesses to foreigners to identify and address any national security risks as the result of the transactions.

Finally, the Office of Terrorism and Financial Intelligence (TFI) uses a variety of statutory authorities and an expertise in illicit finance both to protect the U.S. financial system and advance U.S. foreign and security policy abroad. TFI works bilaterally and multilaterally to improve other countries' anti–money laundering and combating the financing of terrorism (AML–CFT) regimes and increase the effectiveness of international cooperation on terrorist financing and money laundering. Additionally, to combat specific threats, TFI can employ targeted financial measures, commonly called financial sanctions or designations, to freeze U.S.-controlled assets of terrorists, narcotraffickers, proliferators, and the vast networks of charities and companies that facilitate these activities. Through financial sanctions, TFI effectively and publicly prevents these nefarious actors from accessing the U.S. financial system.

What Does Treasury Do?

Located adjacent to the White House and National Security Council, Treasury takes its policy role within the national security process seriously. The Department focuses on its own niche capabilities of macroeconomics and AML–CFT measures. However, since money is fungible, Treasury's interests can extend far beyond pure fiscal and monetary issues. For instance, it cares if a country is sold F–16s or other high-cost items if that country's financial ability to maintain the equipment is suspect. Treasury will likely scrutinize a highly indebted country undergoing a comprehensive military modernization program. As a variant of the guns-versus-butter debate, foreign aid can also alter domestic military expenditures. Treasury is not tone deaf to political and military implications. It does, however, take seriously the second- and third-order implications of fiscal impropriety and poor economic policies.

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Treasury's national security capabilities defy easy categorization. Within the three-legged stool of security, economics, and governance, Treasury's core competencies fall within at least the latter two. While created to avoid the "cylinders of excellence," the 3 Ds (defense, diplomacy, and development) also too often become shorthand for Defense, State, and the U.S. Agency for International Development (USAID), respectively. While Treasury does not articulate its own capabilities in those terms, the 3 Ds provide at least a familiar structure for DOD officials to conceptualize Treasury's national security capabilities and roles.

Financial and Economic Defense. What Treasury calls *targeted financial measures* allow the United States and international community to freeze or seize financial accounts of less savory individuals, organizations, and banks. Executed by TFI, "smart" financial sanctions are targeted against individual bad apples as opposed to entire countries. These are distinct from relatively less targeted sanctions the United States imposes: economic sanctions, enacted to restrict certain types of trade (led by Commerce), and diplomatic sanctions, enacted to restrict international travel and other privileges (led by State).

TFI is concerned with many of the same actors as DOD. It designates individuals involved in money laundering, terrorism and terrorist facilitation, proliferation, corruption, drug trafficking, and other destabilizing actions. For instance, TFI has frozen the assets of Iranian banks, North Korean tycoons, al Qaeda leaders, and Hizballah operatives worldwide.

Treasury's means obviously diverge greatly from DOD's, making this a tremendous U.S. defense capability. Rather than attempting to kill or capture individuals, TFI uses its in-house intelligence office to track money around the world. Bank accounts, wire transfers, and financial transactions all help show that a person, organization, or bank is sponsoring illicit actors or funding the acts themselves. Freezing bank accounts is not a silver bullet that will stop terrorism or drug trafficking. However, these sanctions make it much more costly, difficult, and time consuming for those identified to do what they want. Moreover, by identifying facilitators publicly, these designations can often have knock-on effects beyond the U.S. financial system and can prompt foreign governments to take similar actions. As we all know, slowing down the enemy's decision cycle provides a tremendous strategic advantage.

TFI has a complicated process to designate individuals. Briefly, Treasury's TFI mandate derives from a variety of executive orders and the USA PATRIOT Act. Based on policy priorities, TFI's Office of Intelligence and Analysis tracks people or organizations of national security interest and closely coordinates with the rest of the Intelligence Community. Once a designation packet is complete and approved within the national security process, TFI's Office of Financial Assets Control (OFAC) lists the entity. OFAC also passes this information on to domestic and international governments, banks, and other financial institutions, so they know not to deal with this entity if they want to remain in good standing with the United States and its financial system.

Treasury also helps maintain the economic defense of the homeland, serving as the chair of CFIUS, whose cases can arise due to the nature of a U.S. business (that is, if the company possesses certain advanced technologies or has Government contracts) or the identity of the foreign person (that is, the track record of the person or the nonproliferation record of the individual's country of origin). Operating pursuant to the 1950 Defense Production Act, CFIUS has undergone significant reforms since the United Arab Emirates–based Dubai Ports World's attempt to purchase the port management businesses of major U.S. seaports in 2005–2006. DOD works closely with Treasury within this committee, providing substantive expertise and threat assessments to help the United States balance its free market and national security imperatives.[3]

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Financial and Economic Diplomacy. Treasury's IA officials have long served as U.S. financial and economic "diplomats"—although most work in Washington, with only a handful stationed abroad. Treasury regularly interacts with its traditional counterparts within foreign finance ministries and central banks.[4] Especially in times of financial turmoil or to encourage others to enact or strengthen financial sanctions, Treasury's interactions with heads of state and government are routine. For instance, the largest economies' finance officials began meeting annually in the wake of the 1973 oil crisis and subsequent global recession, soon becoming the Group of Seven. Similarly, a larger group of finance ministers formed the Group of 20, first meeting in 1999 after the Asian financial crisis. Treasury also has attachés within 13 Embassies worldwide, providing targeted expertise and communications in places of national interest.

The Department is the lead agency with authority over the U.S. representatives serving on the boards of the IMF, World Bank, and most regional development banks. Maintaining permanent offices at each, Treasury's close work with both the staffs of the international financial institutions (IFIs) themselves and with the representatives from other countries promotes U.S. national interests and influence on current issues. Just as governments often send their top military leaders to U.S. military schools, their premier economists and future government leaders often serve rotations at the IFIs in Washington. Treasury's diplomacy through the IFIs thus directly promotes U.S. long-term interests.

Relations among these economic officials, at the IFIs and in finance ministries and central banks worldwide, are usually excellent and frank. Many attended the same prestigious economic and business schools in the United States and Europe. In addition, and often as a result, many of these technocrats prioritize the same monetary, fiscal, and financial principles. Having similar economic backgrounds does not eliminate disagreements any more than having shared military experiences. However, these relationships and similar perspectives help improve communication and coordination. As a result, coalitions within the IFIs and among ministries are able to make progress that otherwise would not likely occur. With the largest global capitalist economy and increasingly constrained military resources, U.S. economic and financial relationships are great sources of soft power we should continue to leverage.

Financial and Economic Development. While Treasury's main financial stick—sanctions—is spiritedly touted, its macroeconomic carrots are unsung national security heroes. Effective and efficient governments excel at macroeconomic tasks, such as collecting more revenues than they spend (at least in the long term), paying their employees and soldiers on time, maintaining a stable currency and development-friendly policies, and executing transparent budgets to minimize corruption. Unfortunately, few states that DOD is concerned with (except major powers) do most of these tasks well.

Traditionally, development focuses on microeconomic improvement (for example, employment, projects, and community-based activities), which USAID specializes in. However, when it comes to macroeconomic expertise, Treasury—particularly the Office of International Affairs—is without peer within the U.S. Government. IA monitors and analyzes global economic and financial events and trends. It maintains extensive bilateral interactions with the countries' finance ministries and central banks, while also drawing on expertise from private and public sector scholars and analysts. IA then works alongside public and private actors to develop and promote good economic and financial governance that improves countries' prosperity and stability. Its representatives also brief and help prepare senior Treasury and other U.S. officials on policy and substantive issues, decisions, and international engagements, with many issues focusing directly on economic and financial development. While much of this work is based in Washington, Treasury also leverages expertise and information from its strategically placed attachés to improve development efforts.

Treasury has one small development arm within IA, the Office of Technical Assistance (OTA). Using in-house experts and a meager budget—just $34 million was requested for 2010[5]—OTA officials partner directly with interested foreign governments to help them improve their economic and financial systems. Using embedded advisors and short-term trainers, OTA can assist a great range of governments, including postconflict, fragile, and failed ones. OTA focuses on five core areas: budget policy and management, financial institutions policy and regulation, government debt issuance and management, financial enforcement, and tax policy and administration.[6]

OTA is currently providing technical expertise throughout the world, some of it in support of the highest U.S. strategic priorities. Treasury is providing technical assistance to countries affected by and susceptible to the financial crisis, helping to determine the extent of their financial vulnerability, address immediate crisis-related challenges, and prepare for recovery. OTA advisors in Iraq, working with the civilian and military Public Finance Management Action Group, focus on public finance issues and help improve budget execution. OTA helped build capacity in Afghanistan's debt management office and is helping create processes needed for a future domestic government securities market. In Pakistan, OTA assisted the government in improving its banking supervision and is helping the country create a Financial Intelligence Unit within its central bank.[7]

As the formal U.S. representative to the IFIs, Treasury also has a critical international role in economic development. Whether dealing with the macroeconomically focused

IMF or the microeconomically focused World Bank and regional development banks, Treasury's work alongside these international financial institutions helps to bring expertise, resources, and international legitimacy to developmental challenges worldwide. Combining these capabilities, Treasury helps empower governments to more effectively and efficiently enact their own economic and financial policies, including within IA and TFI areas of expertise.

Why Should DOD Care?

Too often, the Departments of Defense and Treasury operate in parallel universes. This is not without reason, as the two have different core competencies with limited direct overlap. For instance, it is wise that the military is not intimately involved in designing the TARP or new regulations for the global financial system. Treasury's skills are much better used not dealing with Fallujah or leading Partnership for Peace exercises.

However, DOD can and should better understand this Department for at least three reasons. First, unlike other interagency partners with which Defense often engages, Treasury's action-oriented, problemsolving instincts are readily recognizable to military personnel. Filled with professionals forgoing large salaries for government work—again, much like DOD—Treasury officials insist that solutions create measurable, monitorable, and sustainable results. These officials can choose to remain as technical specialists throughout their careers, rather than having an "up-or-out" promotion policy. As a result, the quality and experience of economists at all levels of Treasury are superb. Even when Defense's challenges are not directly related to Treasury's, having similar-minded peers with competencies outside our own can be useful within interagency discussions and debates.

Second, everyone loves money. People want jobs. Governments want more revenues to spend. Foreign militaries want to modernize, and we need military interoperability with our allies. Even nefarious actors—terrorists, drug traffickers, proliferators of weapons of mass destruction (WMD)—appreciate the ease of using Western financial institutions. Treasury, in coordination with the IFIs, helps the United States and international community reach their desired economic and financial ends. By structuring incentives appropriately, money can be a critical warfighting and peace-sustaining enabler.

Finally, DOD should better understand Treasury since the Department's small size constrains what it can proactively engage in. While mighty, the Treasury can only split people and their focuses so many ways. For instance, Treasury's entire Office of International Affairs—its "army" of regional and functional macroeconomic experts—employs fewer than 200 people, including political appointees and administrative staff. Twelve Treasury advisors in Iraq are relatively minuscule in number, yet they constitute 6 percent of IA's entire global workforce. By better understanding what capabilities Treasury can bring to various fights, DOD can help pull information and expertise, especially for problems with which Treasury might otherwise not have the resources to engage.

In sum, for the foreseeable future, DOD will face tremendous challenges dealing with the security implications of failed states, rogue actors, WMD proliferators, demographic shifts, and globalization. Many of these challenges will have critical economic aspects that Treasury colleagues already specialize in. By DOD better leveraging the Department's unique capabilities in economic and financial defense, diplomacy, and development, the United States can more effectively and efficiently ensure the security and prosperity of the Nation for many decades to come. **JFQ**

NOTES

[1] Additional information on the Department of the Treasury is available at <www.treas.gov/>.

[2] See <www.treas.gov/bureaus/>.

[3] See <www.treas.gov/offices/international-affairs/cfius/>.

[4] The New York Federal Reserve ("Fed") serves as the U.S. central bank. While independent of Treasury, the Fed and Treasury work closely together and both interact with foreign ministries of finance and central banks.

[5] See <www.treas.gov/offices/international-affairs/intl/fy2010/budget-FY2010.pdf>.

[6] For a discussion of Treasury's processes to help states build and strengthen their public financial management institutions, see Jeremiah S. Pam, *The Treasury Approach to State-Building and Institution-Strengthening Assistance: Experience in Iraq and Broader Implications*, U.S. Institute of Peace (USIP) Special Report 216 (Washington, DC: USIP, October 2008).

[7] Department of the Treasury, "Treasury International Programs: Justification for Appropriations FY2010 Budget Request," May 2009, vi.