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Chair

The Honourable Robert Nault

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● (1615)

[*English*]

The Chair (Hon. Robert Nault (Kenora, Lib.)): Colleagues, I want to bring this meeting to order and start by apologizing to our witnesses. I'm sure they've been through this many times before—they're supposed to be giving evidence to committee and the committee is somewhere else doing the country's business. I want to start off by apologizing to you.

What we propose to do, colleagues, if it's okay with you, is get our first hour's two witnesses to make their opening comments. By then, we'll have connected with our next two witnesses by video, and we'll give them a chance to give their comments. Then we'll get into questions with all four in whatever time is left. I know that's not the best of worlds, but at this point we don't have a whole lot of choice.

Pursuant to the order of reference of Thursday, April 14, 2016, and section 20 of the Freezing Assets of Corrupt Foreign Officials Act, this is our statutory review of this act.

Before us as witnesses are Milos Barutciski and Vincent DeRose. One is a partner of Bennett Jones, and the other is a partner of Borden Ladner Gervais. Welcome to both of you.

I'm going to go straight to your presentations.

Milos, are you going to start?

Mr. Milos Barutciski (Partner, Bennett Jones LLP, As an Individual): We agreed that Vincent would start.

The Chair: We'll start off with Mr. DeRose, and then we'll follow through. As I said, we'll see how that goes, and then we'll go right to the other witnesses. I see they are appearing here just now.

Vincent, I'll turn the floor over to you.

Mr. Vincent DeRose (Partner, Borden Ladner Gervais LLP, As an Individual): Thank you very much.

First, let me begin by thanking the committee for the opportunity to appear today. I am hopeful that my experience will be of assistance to your review. I also appreciate the opportunity to further refine the Canadian sanctions legal regime. It is an honour to be a voice in this process.

By way of background, I am a partner with the law firm of Borden Ladner Gervais. I regularly advise clients on a range of issues relating to Canada's various economic sanctions. Our clients have included very large sophisticated Canadian companies as well as a number of small and medium-sized enterprises.

I have assisted those clients in developing compliance programs, conducting compliance audits and investigations, determining the legality of potential export transactions, applying for exemption permits, and undertaking voluntary disclosure for inadvertent breaches with the RCMP. We have also had the opportunity to advise foreign companies and foreign nations on Canada's economic sanctions regime.

It's within this context that we've prepared our recommendations and comments today. I should also mention that my partner Jennifer Radford, who also works in this area, has assisted in the preparation of these recommendations. They represent our views based on our experience with our clients, but they do not necessarily reflect the views of our firm or those clients.

It's within this context that we have identified four areas of potential improvement that arise from the challenges that our clients have experienced with the administration of Canada's export controls and economic sanctions. At the outset, I'd like to stress one other point, and it's this. Our recommendations, while they highlight what we believe are some inefficiencies in the system that could be improved, are not directed at the civil servants, or at particular civil servants. In our experience, the civil servants have been extremely knowledgeable, helpful, engaged, and responsive within what we perceive to be the parameters in which they are permitted to act and the resources at their disposal.

Let me turn to four recommendations we would ask this committee to consider.

Recommendation one is to provide Global Affairs Canada with the mandate and the resources to improve outreach to Canadian companies. Many companies in Canada, particularly small and medium-sized enterprises, do not have sophisticated, and what by necessity are often expensive, control systems in place to ensure that they remain compliant with Canada's economic sanctions.

We have seen, first-hand, Canadian companies elect not to pursue lucrative economic opportunities abroad because of the compliance challenges they face. Some easy steps would go a long way, and we'd like to highlight two. In the first place, we should provide written guidance on how programs for compliance with Canadian economic sanctions can be developed and how Canadian companies that have already developed compliance programs could determine whether their existing compliance programs are adequate from the perspective of the Canadian government. Such guidance is provided in other countries, most notably the United States. In the second place, we should provide a consolidated, searchable list of the designated persons and the designated entities as identified by the various pieces of legislation that form the economic sanctions framework. Currently there does not exist a publicly available, up-to-date, consolidated list of all of Canada's various sanctions lists.

Recommendation two is to provide Global Affairs Canada with the mandate and the resources to issue guidance on interpreting the meaning of specific provisions in the implementing regulations. Other jurisdictions, such as the United States and the European Union, issue written guidance on how to interpret particular provisions. Canada does not. The result is that Canadian companies often face a level of uncertainty with respect to compliance that their counterparts in allied countries do not.

● (1620)

While lawyers such as Milos or me can give advice based on what the U.S. or the EU says, at the end of the day, it is not what the Canadian government and the department in charge have told us that they believe it means.

Recommendation three is to provide Global Affairs with the mandate and resources to improve the exemption permit application process.

In our experience, significant delays in the processing of permit applications are too common. To avoid delay, we would urge this committee to consider recommending that a mandatory known period of time be imposed on the determination of permit applications. A known time frame will greatly assist Canadian companies that are anxious to know whether they may capitalize on an opportunity, and assist them in managing their business relationships abroad. Again, on a first-hand basis, there have been too many situations where a Canadian company seeking guidance from the department has had to turn away from opportunities simply because of uncertainty and because they didn't want to take on that risk.

On recommendation four, there currently in Canada does not exist a formal voluntary disclosure program that encourages Canadian companies that discover an inadvertent violation to come forward to bring themselves into compliance. We have had clients elect to voluntarily disclose a breach to the RCMP, and in my experience the RCMP has reacted very positively. That said, clients have elected to proceed in that manner with the knowledge that they are putting themselves at risk. When they elect to proceed in that manner, they do not have the protections of voluntary disclosure that we see in other statutory frameworks within the Government of Canada. The Competition Act is an example of a formal voluntary disclosure process, if this committee wishes to look for an example.

With that, let me close by saying this. Although our recommendations do not provide specific legislative amendments, we believe that they would improve the administration of the economic sanctions regime in Canada.

Once again, thank you for inviting me here today. It's my honour, and I look forward to answering any questions you may have.

● (1625)

The Chair: Thank you very much, Mr. DeRose.

Mr. Barutciski.

Mr. Milos Barutciski: You said it like a native, Mr. Chairman. It's Macedonian, in case you are wondering.

Thank you very much, Mr. Chairman and members of the committee.

Like Vince, I've been practising for the bulk of my 30 years as a lawyer, in the large national firm Bennett Jones for the past 10 years and another firm before that. I did spend two years, in the early nineties, as chief of staff at the Competition Bureau, so I do have a bit of a flavour from the inside of how the administration of enforcement of a regulatory statute works, but I'm going to talk mostly as a representative and counsel to public and private companies and state enterprises. I've acted for a number of Canadian crown corporations over the years. I've also acted for governments, both in Canada and internationally, and have negotiated treaties for the Government of Canada.

Take it from where I come from. I'm going to be perhaps a little less focused on specific recommendations and more critical of the regime. I appreciate that one of the reasons you are looking at FACFOA,, the freezing assets legislation, and bringing SEMA into it is that FACFOA has the parliamentary review provision, so that creates an opening.

I'm not sure how the mandate of the committee works, but I would strongly urge you to look at bringing into the sweep the export and import controls act, because that's part of the same parcel. In fact, FACFOA really doesn't have much to do with sanctions and export controls. From a practice perspective, I can tell you—and we were speaking outside—FACFOA is essentially an afterthought. It's a footnote, when you are advising companies.

Sanctions and export controls are a serious business because of the impact on day-to-day business decisions for large and small Canadian companies. In fact, small Canadian companies, to a great extent, are perhaps the bigger victims of some of the gaps or lack of process that Vince was speaking about.

Let me start very quickly, and I'll highlight a couple of things from the start.

The comments I'm going to make are negative, but they are not “the sky is falling”. It really doesn't take a huge amount to fix it, but the system is fundamentally incoherent. The very fact that we are looking only at FACFOA—as I say, a footnote, an afterthought in terms of its impact on decision-making.... I'm not saying that.... The policy rationale for FACFOA is very important, absolutely. We don't want to become a haven for corrupt foreign officials to park their ill-gotten gains here. I think we are all on the same page, but that's not what really impacts most business decision-making, whereas a regulatory regime that says you have to have permits and treat certain kinds of goods as strategic goods, dual-use goods, military goods, and so forth—chemicals that could be precursors to weapons of mass destruction—that's something that we do. You use certain chemicals for normal, everyday industrial processes that could also be used for things that are far less benign. Those are things that a lot of Canadian companies pay attention to.

When I say that the system is incoherent.... We should be looking not just at the statutes—Export and Import Permits Act, SEMA, United Nations Act, together—but also at the agencies and how they enforce. Perhaps the incoherence.... This is not a criticism of the enforcement officials and the administrators of the act; they do the best job they can with the limited resources they have.

What I have seen, in the 30 years I've been doing this, is that at Global Affairs Canada, under its various names over the years, the sanctions people don't talk to the export control people. It's not that they don't talk because they don't want to; they don't talk because there are only 12 of them. It could be 10, 11, or 13; it varies. Those dozen public servants basically have the job of briefing the minister on crises that have developed, as with the Garretts, recently, who were stuck in China for years. They also brief the minister on policy issues. By the way, that division isn't just sanctions; it's United Nations, human rights, and sanctions. Believe me, sanctions are at the back of the list, because the United Nations and human rights are equally or perhaps more important on a fundamental level. You have 12 people who are briefing the minister, drafting regulations, dealing with crisis situations, and doing policy work. They also have to process permit applications and then make recommendations to the minister. They are not structured to do that. What happens is that they just freeze up.

● (1630)

I'll illustrate this with two simple examples, and I'll leave it at that. In one particular instance, when you seek advice from the export controls bureau.... By the way, the trade and export controls bureau has 50 people, with engineers and technical people who assess products. Say they're dual-used, the encryption is this many adds, 128-bit or 256-bit, or whatever. They have the capacity. They also have an administrative arm that processes permits. There's an online permit processing vehicle that they use, so it's structured to regulate and administer what is a regulatory act. If you call the export and import controls bureau, and you ask for advice, you get advice from informed public servants who are there to administer a regulatory statute.

I asked, “How do you interpret that?” They view it as their job to tell me their interpretation of this clause, what this provision on the export control list in the act or in this regulation means. That's how they apply it. They don't view that as somehow disclosing anything. That's what they do because that helps me and helps my clients process their permit applications, and it makes it easier, to the benefit of everybody, including the public servants.

If I call the sanctions people—and believe me this is no criticism of the individuals or the managers—the answer I get is, “Oh, we can't interpret the law.” I'm trying to remember the words I keep hearing that a lot of us laugh about when we hear. They are, “We can't give legal advice.” I marked it down.

I say, “Well, I'm not asking you for legal advice. I deal with the Competition Bureau. I deal with CBSA. I deal with the Ontario Securities Commission. I deal with any number of agencies, and I will get their take or interpretation of how they administer the act. I'm a lawyer. I'm sorry, I'm not calling you for legal advice, I'm calling you as a regulator.”

They say, “But we're not regulators; we're lawyers for the department.”

I reply, “Well, actually, you are because the statute says the minister is a statutory decision-maker and issues permits. So thank you very much, you are now a regulator, you are not a lawyer to the government. That's another hat. But when you're talking to me and my client, you're a regulator.”

It's the height of arrogance, and, frankly, of dysfunctionality that I get that answer. My clients, if they have the imprudence to call directly, get a complete runaround.

Do I blame those officials? Absolutely not. Those 12 people cannot advise the minister properly on the things the Minister of Foreign Affairs—it's not the trade minister—needs to be advised on in relation to human rights, UN issues, and process permit applications for gas turbines. It's really not the same bandwidth issue.

So there's a dysfunctionality at the level of how the process works. That's the first, the mindset. One is a regulatory mindset. The export controls bureau is properly resourced, by and large. The other is a policy mindset, doing a very important policy job, but does not have the resources to do the other job. It's not just SEMA, but also the United Nations Act, because it's the same process. It's virtually identical in terms of their regulatory architecture, but they don't have the resources or the mindset.

The second example I want to illustrate is a little bit closer to the coal face in terms of enforcement. Vince talked about voluntary disclosures and how we don't have a process for voluntary disclosures. There is a very elaborate process he mentioned at the Competition Bureau. There's a very elaborate process that's set out in departmental memos at the CBSA and many other agencies both federally and provincially.

The controlled goods directorate at PWGSC deals with a lot of the same stuff, military goods, except it's not the export and import, it's the handling of guns, tanks, armoured cars, and ammunition in Canada. We don't want those wandering around loosely on the back of someone's pickup, so they have a voluntary disclosure process that's fairly well articulated and elaborate. While the export controls bureau doesn't have a formal process, we've been doing it long enough that we understand where we're going when we do, more or less. We kind of have the drill.

Let me give you an example that will illustrate what I'm talking about. Just about year and a half ago, I did a voluntary disclosure to.... By the way, sanctions and export controls almost always go together. You rarely find yourself with a sanctions violation that is not also an export control violation. That's what we had. It had to do with a sanctions violation that had been going on for a period of years, and so we made a voluntary disclosure to Global Affairs, the sanctions folks, the dozen hearty under-resourced public servants at that office, to the export controls bureau, and to the CBSA.

● (1635)

If you export goods without the proper permits, you have actually filed an improper export declaration. Therefore, you've committed offences under the Customs Act. You have to do it under all three.

The first answer...the export controls guys get it. It took them about six months to process it and be finished. CBSA pretty much the same thing.

From the sanctions folks, what I was told is, “We can't do anything with it. We'll have to refer it to the RCMP.” I said, “Before you, the sanctions folks at the Department of Foreign Affairs refer it to the RCMP, just pick up the phone and think for a second, because your sister agency two floors up, or in the other building, is examining the very same facts. There's something that's not quite right and, perhaps, not the best use of the government's scarce resources for you to re-punt it to the RCMP, when they know even less about sanctions than you guys do.”

In what I think is a great credit to them, they didn't punt it to the RCMP, and we went through the process with CBSA and the export and import controls bureau and we finished. We got the sign-off letter saying, “No. Thank you for making the voluntary disclosure.” It was basically that we did the right thing and they were going to essentially close the file. We did the right thing. We cleaned it up. We fixed it.

Then I asked the sanctions folks, “Can I get closure?” Their response was, “You know, we really don't know what to do, so we're going to refer it to the RCMP.” That's six months later. So the benefit or the rational decision that was made six months before kind of evaporated. They had no process to bring it to closure, or the resources to bring it to closure, so it was referred to the RCMP.

Thankfully, by the time it went to the RCMP, I spoke with my contacts there who I deal with regularly and I said, “Guys, this is a sanctions and export control issue. You've seen the report you have from your colleagues at foreign affairs. Leave aside the sanctions and the export controls. We've gone through the same facts, just through a different regulatory lens. Do what you think makes sense. I think it would make sense to basically follow their lead because you're not the sanctions and export control experts.”

That's what held it up until, ultimately, the RCMP stepped in. But it was a year-long process that made no sense and hence the incoherence. None of these agencies talk to each other. The client is paying for and Canadian business is paying for and taxpayers are paying for four disjointed, disconnected, duplicative, overlapping processes that, at various times in this, went in different directions and then had to be nursed back into sync.

That's what I'm leaving you with. It's great that you're starting with FACFOA and that gives you the statutory mandate to look at this, and it's good that you've looked at SEMA, but the issue is actually.... Let me put it this way, it includes.... I hesitate to raise this, but I testified at the Standing Committee on Human Rights about six months ago on the arms treaty agreement and the export of military goods, and it's the same thing. That's yet another process that deals with the same issue, except in a very particular product category, namely, military goods, which are caught by these regimes. It's caught by the export permit because it's schedule 3 of the export control list.

What I'm urging you to do in your report is by all means take what Vince and I and others have said and step back and look at how the coherence of Canada's export regime across multiple platforms can be improved, including the recommendations that my friend made earlier.

Thank you, Mr. Chairman.

● (1640)

The Chair: Thank you.

What I'm going to do, if our witnesses at the front are willing, is go right to our other witnesses who are on video conference.

In front of us is Melissa Hanham, senior research associate, James Martin Center for Nonproliferation Studies at the META Lab, Middlebury Institute of International Studies, and James Walsh, senior research associate, MIT Security Studies Program.

I don't know who has decided to go first, but since Melissa is at the top of the list she gets to go first. Melissa, would you like to start?

Ms. Melissa Hanham (Senior Research Associate, James Martin Center for Nonproliferation Studies, META Lab, Middlebury Institute of International Studies, As an Individual): Thank you very much for having me, Mr. Chairman. I am deeply honoured, as a Canadian living in the U.S. now, to be part of this committee hearing. I hope I can be of use.

Unlike my previous colleagues, I am not a lawyer or a legal scholar. I'm a researcher at the Middlebury Institute of International Studies at the Center for Nonproliferation Studies, and my expertise is North Korea and how it procures different items, particularly dual-use items, that can be used in its WMD—weapons of mass destruction—program as well as in its delivery devices.

I hope I can shed some light on how North Korea maintains networks and launders money to procure these items. I looked through FACFOA and SEMA, and I also took a stab at making some suggestions there. I hope you'll be patient with me, as I am more of a layperson than my previous colleagues.

From my study of the Financial Action Task Force's recommended guidelines, I find that FACFOA is clear, coherent, and well designed. It may be yet another instrument in addition to many other instruments, but it's a very important loophole we need to close.

North Korea is among one of the most notorious money launderers when it comes to proliferation. The Financial Action Task Force itself has only been looking at the issue of proliferation finance for the last few years, so I really am impressed that Canada has been on the forefront. Not all countries have adopted recommendation seven in their guidelines yet, so Canada should be proud of doing so.

I saw two areas that may be useful to mention. One is the term “foreign state”. In both FACFOA and SEMA, the term “foreign state” is frequently used. I understand that there is a political reason for doing so, but I would recommend perhaps using the language “jurisdiction” instead to capture areas such as Taiwan, which have high-technology exports and trade with Canada but are not recognized as foreign states by Canada.

This type of activity has been exploited in the past by North Korea. Although the jurisdiction of Taiwan has worked hard to improve its own laws to handle export controls, North Korea will likely continue to exploit Taiwan, potentially as a transshipment country for goods coming from elsewhere, including, potentially, Canada.

A second point, which I think is really interesting to look at, is the reference to NGOs. I work for an NGO, and I'm very proud to work for an NGO. In particular, I have a lot of respect for NGOs that help in development, human infrastructure, agriculture, and life-saving activities in crisis situations. I'm very pleased to see that Canada has been included in an exception for them, particularly with regard to medical equipment. However, I recommend that this also be accompanied by some guidance on how NGOs interact with these particular activities in North Korea.

North Korea is an area that has previously exploited foreign NGOs to receive dual-use goods, particularly biological dual-use goods. An example of this is the United Kingdom's CABI. This organization has been exploited in the past. They offer to provide training and equipment on producing biopesticides for use on crops. The equipment by itself falls below the threshold of what would be controlled according to export control laws. However, the training they've provided is a dual-use good. In this case, they were teaching them how to make a bacteria called *bacillus thuringiensis*, which is equally useful when making *bacillus anthracis*,which is the bacteria that causes anthrax.

● (1645)

These equipment and training activities were later found related to North Korea's biological weapons program in a facility known as the Pyongyang Biotechnical Institute.

On the subject of how sanctions should be used as a tool in foreign policy, I had a few comments there. First, sanctions cannot prevent a WMD program alone. They are not a single tool in the pallet of tools we have. In fact, they may not even be the best tool. I do not believe personally that they are useful as a punishment or as some kind of inducement to encourage a state to return to diplomatic negotiations. However, in this case, particularly with North Korea, I find that sanctions are a somewhat useful tool in slowing the development of the WMD and delivery system programs that North Korea has. It is perhaps mild solace to people who are concerned about the state of North Korean citizens who are impoverished; however, particularly for military or dual-use items that can be used in nuclear, chemical, and biological weapons programs or delivery systems such as missiles, I believe it is important enough that sanctions are used as a way to slow the development of those programs.

North Korea has a very complicated system of evading sanctions, and it has been very successful in evading U.S., EU, Canadian, and UN sanctions in the past. They have advance money-laundering techniques as well as very simple “suitcases full of money” techniques. They have used flags of convenience in the past. They have used front companies located within and outside of their own borders. They have even used their own diplomatic embassies as locations for receiving goods that can be used in WMD programs. That makes your job extremely difficult, and it makes me very sympathetic to Canadian businesses that must contend with these types of tactics.

I agree with my previous colleague who said that additional guidance is very useful to companies in meeting those types of recommendations. While working here at the Middlebury Institute, I have done quite a few industry outreach programs with my colleagues in our export control department, and I find that companies welcome these types of activities. If the Canadian government does not want to participate in these activities alone, you may want to rely on civil society and academia to assist you in doing outreach on these types of topics.

North Korea's WMD program is now very advanced, with five nuclear tests, and increasing missile tests. I don't think diplomatic activities should be focused on denuclearizing the peninsula anymore. Now we need to focus on preventing additional nuclear tests, additional missile tests, and the additional production of fissile material. The way that sanctions may be useful would be to focus on those choke points that provide equipment, training, and knowledge that support those particular programs. I recommend in particular that the export regulations, which I understand are separate from what we are talking about today, focus on the use of computer numerical control machines, electronics, and ball bearings that are too expensive for North Korea to make in its own industry; chemical reagents, fuel and oxidizer; heavy machinery such as construction equipment and logging trucks; metal alloys that can be used in centrifuges or missiles; in addition to biological equipment such as bioreactors, fermentation, spray dryers, and safety equipment that would be used in a WMD program like level three safety cabinets or suits that protect scientists.

In addition, cyberwarfare is becoming a very important component of our fight against WMD. To this extent, encryptions software, both defensive and offensive, should be looked at by companies that are intending to export to the region or even to a third party that may transfer that information to North Korea.

● (1650)

I believe some of the recent export control cases that have popped up in Canadian media are largely around cases where a company has exported to a third party, perhaps an unknown party, likely in China, and that export has been re-exported to North Korea. That is, of course, not Canada's issue alone, but I do believe that by working together in enforcement, we can better improve the relationship between the enforcement mechanism and the legal mechanism. Enforcement is, perhaps, the most challenging part of the whole process, but I understand that is beyond the scope here, so I will leave it at that.

Thank you very much for having me here, and I welcome all your questions.

The Chair: Thank you very much, Ms. Hanham. I'll go right to Mr. Walsh for his comments, please.

Dr. James Walsh (Senior Research Associate, MIT Security Studies Program, As an Individual): Mr. Chair, Madam, Vice-Chairs, and members of the committee, it's an honour to be with you here today. My only regret is that I am not in beautiful Ottawa with you. If I look a little green around here, it's not only the fault of the video conferencing and it's odd lighting, but it's also because I came down with food poisoning yesterday. Food poisoning was not going to dissuade me from appearing before you.

My testimony is based on more than 15 years of research on both North Korea and Iran. I've travelled to both countries, and with my colleague John Park, a Canadian, recently completed a three-year study on North Korean sanctions based on interviews with North Korean defectors whose jobs were to procure licit and illicit goods and materials. I filed a copy of that study with your committee.

Before addressing some of the the important questions posed by your committee, let me comment on two common errors one finds in the discussions of sanctions. First, sanctions are a tool that can be used to advance very different policy objectives, but most discussions of sanctions mix together different goals and objectives, leading to poor analysis and faulty evaluations. Sanctions can, among other things, be used for the denial of technology and goods, coercion, bargaining, punishment, inducing regime collapse, and deterring others who might want to imitate a target country. These are all very different things. Some of these objectives are far more difficult than others, and some are contradictory, for example, with bargaining and regime change. If you tell a country your objective is regime change, they're probably not going to be interested in bargaining with you. An effective sanctions strategy requires clarity about the objectives.

In addition, at a time when sanctions are offered as an answer to virtually every problem, it is easy to forget that sanctions, by themselves, will not accomplish policy objectives. They are one limited policy instrument that can be useful in combination with other tools as part of an integrated political strategy. Sanctions did not stop the Iranian program. The Iranian nuclear agreement stopped the Iranian nuclear program. Sanctions, together with other conditions, helped make that agreement possible, but without a negotiation, Iran would still have 19,000 centrifuges. Punishment for the sake of punishment, in the absence of a political strategy, may be psychologically and politically satisfying, but it does not solve real world problems.

Now to your questions. The first question is, how has the use of sanctions evolved over time? In the last decade or so, sanctions have witnessed an unprecedented level of innovation. This has included targeted financial sanctions, America's use of its position in the international banking system to impose extraterritorial sanctions, and the designation of individuals, government ministries and organizations, and non-state actors. These innovations have been impressive, but two caveats should be kept in mind. First, to date, the research has not shown that these new forms of sanctions are more effective than the older versions. That might yet be demonstrated, but the jury is still out on that one. Second, we are not the only ones innovating. As they say, the enemy gets a vote, and the targets of sanctions have not stood still. They have innovated and developed countermeasures. In the case of North Korea, it can be said that Pyongyang has been quicker to innovate in the face of sanctions than the international community has been in responding to the DPRK's countermeasures.

Your next question is, how effective are sanctions in compelling behaviour on the part of state and non-state actors, and in deterring or denying specific activities? The short answer is that sanctions have been useful in some cases and not in others. Overall, the research suggests that sanctions can be effective, but they are successful in roughly less than half the cases studied. It depends to a very large degree on the conditions: who is being sanctioned, for what reason, toward what purpose, and the degree to which the sanctioned party depends on international commerce. It is important to distinguish between imposing costs on a country, which is easy to do, and changing the behaviour, which is much harder to do. For many years, the U.S. was able to impose costs on Iran, but that did not change its nuclear behaviour. Indeed, it went from having roughly 300 centrifuges to 19,000 centrifuges during that period of sanctions. Too often, policy-makers judge the effectiveness of sanctions by triumphing the costs imposed, such as inflation and lost GDP, rather than whether one is any closer to achieving the policy goal of changed behaviour.

The next question is, to what extent are the cases of Iran and North Korea comparable from a sanctions standpoint? Simply put, not very. First, there is no country like China in the Iranian case, i.e., a country with tremendous leverage, but one that also has the ability to insulate the target. That just doesn't exist in the Iranian case.

● (1655)

Second, Iran depends on international oil sales, while North Korea relies primarily on the sale of coal and commodities to one country, China. Because of the global nature of oil sales and Iran's close ties to the international financial system, it was vulnerable to the application of targeted sanctions.

Third, while Iran's government has authoritarian aspects, it cannot simply ignore the conditions of its citizens without political consequences. By contrast, the DPRK is a dictatorship unafraid to use any measure to suppress its population.

Your next question was, are unilateral sanctions more or less effective than multilateral sanctions? The research suggests that, on average, multilateral sanctions are more effective, but, again, it depends on the circumstances. North Korea provides an obvious example. Ninety per cent of its trade is with China. China has more leverage on Pyongyang than the rest of the international community combined. In general, however, and for obvious reasons, multilateral sanctions have been more effective insofar as they narrow the options of the target state.

Last, in what ways do sanctions imposed have an impact on the citizens, economies, and elites of targeted states? This is a vitally important question that is too often overlooked by policy-makers. In our study of North Korean sanctions, we identified a number of possible unintended consequences. Some of them were negative, some were positive, and with some it was hard to judge in which direction they would have an effect.

Curiously, we documented that in North Korea some sanctions actually had the effect of improving Pyongyang's procurement capabilities. Facing higher risks than costs, North Korean traders resorted to paying higher commission fees to their private Chinese middlemen, with the effect that Pyongyang was able to attract larger, more sophisticated partners.

Our main fear, however, is that squeezing the North Korean economy will have an adverse impact on the lives of millions of North Korean citizens who already live on the economic margins. Our concern applies to the macro level—for example, curtailing coal exports and remittances, something that is the subject of today's UN Security Council resolution. At the micro level, South Korean sanction laws make it more difficult for humanitarian NGOs to operate in the DPRK. We are not confident that governments can precisely dial in economic pressure and know for sure whether it will cause pain or cause a humanitarian crisis. We think that's worth keeping an eye on.

In summary, sanctions can contribute to achieving foreign-policy objectives, but they are not a wonder drug. It is easier to impose costs than to change behaviour. Often, they have no impact, and in some cases they can actually have severe negative consequences, as was the case with the Iraqi people during the Iraq sanctions in the 1990s. When they are effective, they are part of an integrated political strategy that has a clear objective, not a stand-alone measure. More so than most foreign-policy instruments, they depend very much on the particular conditions in play.

Sanctions can play a useful role, but if they are misapplied, oversold, because the tail wags the dog, or are confused in their application, the results can range from simply being ineffective, to inhibiting a political solution, to harming civilian populations. Knowing the difference between where sanctions can be helpful and where they are harmful will require tough questions and attention to detail.

Thank you for the honour of appearing before you today.

● (1700)

The Chair: Thank you very much, Mr. Walsh. I'm sorry for your illness, but you managed to survive it all. Good for you.

We are going to start right off the bat with Mr. Kent.

Hon. Peter Kent (Thornhill, CPC): Thank you, Chair, and my thanks to all of our witnesses today.

I have two questions I'd like to ask to Mr. DeRose and Mr. Barutciski.

No doubt you're aware, from having looked at the minutes of previous meetings, that we've had testimony saying the Canadian sanction system is broken and the U.S. sanctions enforcement system is the gold standard. You have spoken about dysfunction and incoherence.

You didn't speak, other than indirectly, about the delisting, how you inform yourselves when entities, individuals, or third parties are taken off a sanctions list.

I'd like to have you speak, if you have experience here, to the situation that occurred when the Iran sanctions were eased somewhat when the new Liberal government came to power last fall, a year ago.

The government couldn't, or wouldn't, answer questions in the Commons, in question period, about who had been taken off the list. We learned later that one of the Iranian state banks was delisted. In doing that, we found that individuals had to go to American sources to compare sanctions lists to find out who was actually on or off.

I wonder if you could speak to that and how you, yourselves, inform your respective companies, or how the community informs itself in the absence of a consolidated list and the public list on delisting?

Mr. Milos Barutciski: I'm not sure which metaphor to use, high school spin-the-bottle or the more adult and a little sharper Russian roulette, but there's a bit of that.

Let's start with delisting. It's impossible to talk about delisting without the flip side, which is how they got there in the first place. They're equally non-transparent processes. On one level, you understand why: you don't want governments, when they list somebody as being active in, take Iran, somehow affiliated with the Iranian national guard and very active in the proliferation of the nuclear program, the military nuclear program. You don't want to disclose intelligence sources and how you know that, so I get the reason for being a bit more circumspect. Let me give you the back end, and it's the same thing on the delisting.

You're saying the more recent government; I'll give you another example going back to when these sanctions were first introduced by your government six years ago. One of my clients, a Canadian company that was exporting medical equipment to Iran, to a particular company there, found itself on the list. I represented them. It took a year and a half to get them off the list.

The right I have as a listed company is to ask the minister why I'm listed. One of the things they told me right at the outset was that there was reason to believe the company was involved in the delivery of weapons of mass destruction. The company was basically in the process of importing dialysis equipment and various other things such as that. I don't know, but I'm guessing that catheters might not be the most efficient means to deliver weapons of mass destruction. I'm not an expert in WMD, so I'll leave it at that. However, it took a year and half to get through this process. The irony was that the very first call, literally, was within a week of the sanctions being promulgated in July 2010.

My client, the owner of the company, is a Canadian citizen, an Iranian Canadian citizen. What he told me was, "Oh, and by the way, we're one of the few Iranian companies that OFAC"—the Office of Foreign Assets Control, the so-called gold standard in the U.S. —"licenses American companies to export to." When I finally had to deal with the Department of Foreign Affairs, my conversation went a bit like, "Okay, what do you guys know that the CIA doesn't know?"

I have my suspicions that what happened was somebody pulled a list from CBSA and said, "Okay, who's exporting to Iran? Who's importing from Iran? Boom, put them all on the list." My gut tells me that may have happened, having been around this a lot before. It's not so much the lack of transparency that's important, it's the point that James Walsh made earlier, which is that sanctions work when there's a coherent reason for doing this particular thing. If what we're doing is imposing sanctions, or lifting sanctions—because it works both ways, the listing and the delisting—because it's a good political statement, you're making a good political statement. As Mr. Walsh said, you might also be imposing costs on the target. However, I can assure you that you're also imposing costs on Canadian businesses.

When I'm looking and trying to figure out why company X is on the list, or why individual Y is on the list, and trying to advise a client because they've come up in some search, you know what, I don't know. When you're imposing costs that way on yourself, the best analogy I can say is that I think it's more Russian roulette. What you're doing, for no cognizable reason in terms of why you're focusing on this person, is basically taking yourself, Canadian business, and grabbing yourself by the throat, putting the gun to your head, and saying, "Comply or the dummy buys it." It's kind of silly.

● (1705)

Hon. Peter Kent: Your example seems to speak to the siloed effect of the different agencies and departments.

Mr. Milos Barutciski: Exactly, and the disconnect between the political rationale for doing it and the assessment or evaluation of what is actually being done.

Hon. Peter Kent: Mr. DeRose, could you speak to this?

Mr. Vincent DeRose: Yes, I'd be happy to.

Maybe I would take a slightly different twist. You asked about delisting. By way of example, if you take Russia or Iran, when they were recently delisting, without the consolidated list that we have urged be created at least for a week, two weeks, or a month, it's tough to figure it out. Quite frankly, the way you need to go through it is to find the latest consolidated regulations with the last known list, and then go through all the amendments that have been issued, and you literally have to have someone remake the list. It's not impossible, but if we look at earlier this year, when the Canadian sanctions against Iran were lowered, we had an number of clients calling us wanting to know who they can do business with. We had a team at our law firm going through and doing it, and these are people who are used to it. A Canadian company out there that does not have that experience, quite frankly, would be at a loss.

The Chair: Thank you.

I'm going to go to Mr. Fragiskatos now.

Mr. Peter Fragiskatos (London North Centre, Lib.): Thank you, Mr. Chair.

Thank you to the witnesses.

My first question is for Mr. Barutciski.

You're saying that this problem didn't appear yesterday. This is something that you've noticed over a number of years. When I say "this problem", I mean what your testimony pointed to: the lack of resources. I think you said that there are between 10 and 13 officials working on the sanctions portfolio. So, this is a long-standing problem? Okay.

● (1710)

Mr. Milos Barutciski: We kept nine.

Mr. Peter Fragiskatos: Okay.

To Mr. Walsh, actually, the substance of my questioning will focus on this.

Traditionally, sanctions have been imposed when there are violations of international peace and security, which can, depending on how one defines that concept, encompass human rights violations. However, now there is an emerging view among some —at least in Canada, and certainly in the United States—that urges policy-makers to put in place sanctions that are clearly in response to human rights violations. It's gone this way in terms of the Magnitsky Act. Certainly, there have been discussions in this committee, in part, because of what we've seen in the United States.

I wonder, with all your expertise in the realm of sanctions—and I'll put the question to Professor Hanham, too—could you speak to this? Could you offer any advice to the committee? Should we be looking at putting in place a change to the existing legislation, so that sanctions are imposed whenever there are violations of human rights? What's the threshold? What kinds of human rights violations ought to qualify? If you could also mention intended and unintended outcomes in your answer, that would be very useful.

Dr. James Walsh: Thank you very much for that important question.

Let me preface my answer by saying that I am primarily a security studies person who focuses on nuclear non-proliferation. But, being in security studies, I have had occasion to speak with colleagues about this issue. I'm working on Iran and North Korea, and North Korea has a horrendous human rights record.

Let me also make clear my full personal and professional commitment to the concept of human rights. I think it's fundamental and basic—more basic than other things that we emphasize every day. I think human rights may be more important than democratic practice, for example, but there's a big argument there.

Let me jump to the last question, and then move up.

With regard to outcomes, I would really encourage people to look at the research on the relationship between sanctions and human rights outcomes. Abuses of human rights are bad. Sanctions are punishment. But, fundamentally, you have to ask yourself, are you doing good? Are you advancing the goal in a practical manner, or are you making things worse, rather than better?

If sanctions have unintended negative consequences for the very communities you are trying to protect, then perhaps you should look at alternative policy tools and not sanctions. Again, this has not been the focus of my research, but the reason I say this is because I am certainly aware of research, some large and quantitative studies, that suggests that there's a very negative relationship between the imposition of sanctions and human rights outcomes. The arguments go something like this. Let's assume there's a dictator involved here. When you impose sanctions for human rights purposes, it makes the dictator become more nervous about his political situation. The dictator may feel a need to crack down on the domestic population, and it also gives an excuse for cracking down on the domestic population. Those are general propositions. They could be true in some particular cases and not in others. But I say, let evidence be our guide.

Remember what I said about North Korea or about non-proliferation sanctions, in general? This is something that is maddeningly a matter of “the devil is in the details”. For some countries, sanctions are going to work great. For some, they're going to be terrible—and by “terrible“, I mean not effective. In some cases, they might actually cause more harm than good. It really comes down to particular countries and then to particular situations.

But—

Mr. Peter Fragiskatos: Professor Walsh, what you're saying is very interesting, but since my time is limited, I'd just like to ask a follow-up question.

Even in cases where the sanctions policy is written so that there are asset freezes, travel bans, etc., is it restricted? We're not talking about the imposition of sanctions on a wide scale? You're still talking about real, potential, harmful circumstances being imposed. You talk about that providing an excuse to an authoritarian regime to exert all sorts of human rights abuses. That's what I take from your statement.

Could you follow up on that?

Dr. James Walsh: Yes. I will be brief this time. I'm sorry.

I said that's a possibility, so my advice to policy-makers would be to provide the executive with some discretion when you have statutes like this; don't make them automatic.

Also, people should do their homework. They should look at what the data says and they should say, “the way this country acts sure looks like a bunch of other countries that we've sanctioned before”. Have those sanctions worked or have they made things worse? Then they should keep an eye on it. Don't just impose it and leave it forever. Try to give yourself some room to correct errors or to adjust. Many times regarding sanctions legislation, once you're in, you're in for a dime, in for a dollar and it's hard to get out.

I would say, practise discretion and follow the evidence by relying on the data.

Mr. Peter Fragiskatos: In my remaining time, I'd like to ask Professor Hanham about her thoughts.

Ms. Melissa Hanham: In large part, I agree with Dr. Walsh. I do think that blanket sanctions almost always have negative consequences, simply because they punish those people who are already suffering the human rights violations themselves.

For example, in North Korea, when food aid came in, it would be sold among the elites on the black market. Different activities are used to circumvent aid efforts, so those people at the bottom are the ones who are facing the brunt of it.

I do think targeted financial sanctions and travel bans may be of use and may be of interest, if they target those people who are controlling the flow of funding. However, I don't think that there is enough intelligence in North Korea, for example, about which companies or who those individuals are, to do it in the targeted way that people truly want to.

I do think that you could adjust, but it would almost always be a game of catch-up.

● (1715)

The Chair: I'm going to go Madame Laverdière, *s'il vous plaît*.

[*Translation*]

Ms. Hélène Laverdière (Laurier—Sainte-Marie, NDP): Thank you very much, Mr. Chair, and thanks to the witnesses for their presentations which were different but all very interesting.

I would like first to make a comment about human resources.

Mr. Barutciski, I was not surprised by what you said. In this committee, we have even heard that the RCMP is not prosecuting. In 25 years, there has been just one prosecution. Since it does not have the necessary resources, it is at the bottom of their list.

This does not happen very often, but I will tell you a short story from my own experience.

I spent 15 years at Global Affairs Canada. In a unit that I headed, there was a small group of three people responsible for liaison with Parliament and cabinet, while other departments had 15 people doing that. Yet we produced the most memos to cabinet. The legacy I left behind was the creation of a special unit responsible for those matters. There is no doubt that I understand the shortage of human resources very well.

That said, the mandate is also important, especially for lawyers when they cannot get one for one thing or another. Is there something specific that our committee should recommend regarding mandates?

Mr. Milos Barutciski: Thank you for your question, Ms. Laverdière.

I will take the opportunity to add my comments to those of Professor Walsh and Professor Hanham regarding the purpose of sanctions. I will also talk about human resources and the mandates that you and others have talked about.

First of all, the purpose of sanctions is quite simple.

I will speak in English for a minute and will then continue in French.

[*English*]

Professor Hanham and Professor Walsh made it perfectly clear. We didn't touch it. We looked at it from a purely business perspective of the costs being imposed on our client, but they made it perfectly clear that the objective of the sanctions, when they're targeted at the kinds of abuses of human rights that go on in North Korea or the proliferation issues that were going on in North Korea and in Iran until the agreement was signed and so forth—there are really important issues at stake.

What happens with the sanctions regime is that we do a bit of what Professor Walsh said. We, as the administration, the government, impose sanctions and then move on.

In a sense, you've outsourced the enforcement to the business community, but our clients, and neither Vince nor myself, have the resources to figure out whether so-and-so in Tehran or in Bandar Abbas is somehow related to the Iranian national guard or some other person with sanctions. We really are spinning the wheel here.

The other point that Professor Walsh made was that once you've committed to the sanctions, it's a really tough political act to ratchet them down or ratchet them up. It's a political tool that's very difficult to meter to specific articulated objectives.

[*Translation*]

I will get back to your question about mandates now.

Ms. Hélène Laverdière: First, I would like to clarify the situation, for public servants in particular.

Mr. Milos Barutciski: That is exactly the question. Whether we have a mandate and ...

[*English*]

if we have an objective and a purpose, a mandate

[*Translation*]

derives from the objective of a particular sanction. Public servants must understand what the objective of Parliament or the government is in enacting legislation or regulations.

Ms. Hélène Laverdière: Let me clarify this.

I was thinking in particular about the issue of the mandate.

The answer could be, for instance, that we do not provide a legal opinion, or something like that. As to the mandate that public servants have to meet your needs, my question is the following. What do they have the right to do or not do?

● (1720)

Mr. Milos Barutciski: That is not a new question. It is a question that arises for any federal public servant at the Competition Bureau, Canada Revenue Agency, or the Canada Border Services Agency. These are regulatory agencies.

If you don't mind, I will continue in English.

[*English*]

A regulatory agency is exactly that. It administers and enforces a regulatory regime and that's what this is. Administration isn't just we promulgate it and if we happen to catch you, whether we blunder into it by error or accident, we enforce you, but it also involves administration of an act. When you talk about mandate it's important that.... And that's what I was complaining about; I was whining, to be honest, about my friends at Foreign Affairs who feel...it's not that they don't feel they have a mandate because their sister agency in the export controls understands that and deals with that. It's a resource problem. Every administrator, every agency that administers a law of Canada or of any of the provinces, understands that it needs to engage with the people the law impacts.

We're not asking for legal opinions, we're asking for guidance on how you do it, which links to the point I was trying to make earlier. It links to the objective of what you're trying to achieve and some of the objectives are extremely important. On proliferation of weapons of mass destruction, I'm hard pressed to think of a more important issue than that from a geopolitical perspective, but you can't deal with that by saying we're going to pass on that, now let's move on to pipelines, or let's move on to human rights and whatever, and you guys sort it out. You know what? Even the biggest multinational is doing the kinds of things Vince was talking about, trying to figure out what this is. The guidance from the administrators that Vince and others have talked about is fundamentally important.

[*Translation*]

There are public servants who can indeed give information, provide guidance, and administer the act.

[*English*]

The guidance is based on the objectives of the act and the objectives have to be tied to the kinds of things Professor Walsh was talking about.

Mr. Vincent DeRose: Could I add two very quick points? First of all, I have not come across a client, a Canadian company, that does not want to comply with the law. They want to comply, and if they are calling me it's because they are unable to figure it out on their own. When we talked about my recommendations, we were very careful. I used the wording “give them the mandate and the resources”, and from my perspective it is the mandate to give not legal advice, but regulatory interpretive advice, and to give them the resources to be able to do it so you can help Canadian companies that want to be in compliance, ensure they are in compliance, and allow those Canadian companies to go abroad and enter into legal business deals. That's what they want; and at the moment, to be honest, many Canadian companies are hitting a roadblock.

It's too bad because we are losing competitive advantage to countries such as the United States or the EU because if you can't buy from Canada, you go to the United States or the EU.

The Chair: Thank you, Mr. DeRose. We have time for one more question

Mr. Michael Levitt (York Centre, Lib.): Is it a short question?

The Chair: Not necessarily short but the usual time and then we have a vote. The bells started to ring a while ago. Our vote is at 5:45, so we have five minutes for Mr. Levitt or Mr. Miller, and then we'll have to call it a day or the whip will do us all in and we'll never be here again. I move over to Mr. Levitt.

Mr. Michael Levitt: I have a question for Ms. Hanham, but there's a disconnect that I want to ask Mr. DeRose about. We've heard there have been about a dozen investigations, and I think two or three findings or prosecutions under SEMA in the whole time. Given the lack of clarity, given that companies are not sure what's going on, how do you account for that, even with all of that and the lack of information? Is it because companies are risk-averse and they're just backing away entirely? It's not as if they're falling into the black hole; are they just staying away from it?

Mr. Vincent DeRose: I would say that there are three reasons. Some simply back off because they are risk-averse. Some will determine what they believe to be compliant, and they will proceed. In terms of why there have been so few prosecutions, again, I would personally suggest that it is more because of a lack of investigations, a lack of resources, and the lack of an ability to investigate. If you look at our allies, take the United States as an example, they have prosecutions every day. Those companies are not acting in a different manner than Canadian companies, but there is not the same level of prosecution. There is no doubt.

● (1725)

Mr. Michael Levitt: Do you think on the pecking order of what the RCMP feels is probably priority in their domain, that this is probably way down the list? Given the sorts of investigations on the sorts of issues that have come up, there haven't exactly been earth-shattering reaches.

Mr. Vincent DeRose: You're putting me into the shoes of the RCMP commissioner. I'm going well beyond that of a lawyer, but I'll say this. If I was the RCMP commissioner, and I was told I could only conduct one investigation a year across all of Canada, would I pick this area? Probably not. Is it important that economic sanctions be investigated and enforced in Canada if you want them to have meaning? They have to be.

Mr. Milos Barutciski: I agree with what Mr. DeRose said, but very simply, enforcement and compliance go hand in hand, and to convince companies that they need to comply, it's not just saying we've got a law. You need to actually be able to engage them, and if the administrator, the agency, doesn't engage, which is what the problem is in the sanctions area, then it's a vacuum. Large public companies with deep compliance cultures, like Canadian banks, just walk away. They don't want to touch it. They will not go anywhere near Iran, even though the sanctions have been fundamentally eased, essentially.

On the other hand, you have a lot of very compliant but ignorant companies, and they see that there's no enforcement. They see they don't have the resources, especially SMEs. They see an opportunity in the oil and gas services sector—not the big producers; I'm talking about the service guys, which are often smaller companies—and off they go. Unfortunately, off they go in a very ill-informed way, and part of the reason is that there's no guidance. So it's not a chicken-and-egg issue; the compliance needs to go with resources and engagement.

I like to talk about engagement more than I talk about enforcement or regulation.

Mr. Michael Levitt: I'm just going to stay with this because I don't think I have time to go to the other part of the question. Sorry about that. You mentioned help for small and medium-sized business, which obviously, in terms of the economy, is important. What other jurisdiction do you feel is handling this well and effectively? Who's doing a good job on this front?

Mr. Vincent DeRose: Let me give you one example that builds on one of our recommendations, which was the consolidated list. If you're in Europe or if you're in the United States, if you're an individual, if you're an SME, you can go to the government website, and you can click on one link, and you can put the name of the person that you are about to enter into a transaction with, and you can hit “enter”, and much like Google, it will pop up, and it will give you a list telling you whether there's a red flag, and it will let you know whether you need to investigate further.

That does not exist in Canada, so if I have an SME, I have to make a decision about going through all the regulations myself, which is extremely complicated and no one will do, or I risk it, or I try to go out and pay a third party service provider, which is incredibly expensive.

So in my experience, lots of SMEs, particularly in the oil and gas service industry, of which we have so much knowledge that we can offer the world, just sort of shrug their shoulders and say it's just not worth the risk.

The Chair: Michael, thank you.

Thank you very much, colleagues. We've now have a grand total of about 15 minutes or so to hustle up for the vote.

I want to thank all four of our witnesses today. Again I want to apologize for our tardiness. Unfortunately, things do happen this time of year in the House, and we're into a multi-vote kind of process this week.

This was very informative. I want to encourage you to give us some recommendations, as Mr. DeRose has done. I think it's very useful and very helpful in the discussion.

On behalf of the committee, thank you very much for spending this time with us.

Colleagues, the meeting is adjourned.

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