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# The American Sanctions on Banks and Financial Companies and Their Effects on The Monetary Stability of Iraq

Prof. Dr. Wejdan Falih Hasan



Al-Bayan Center Studies Series

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# The American Sanctions on Banks and Financial Companies and Their Effects on The Monetary Stability of Iraq

Prof. Dr. Wejdan Falih Hasan\*

## I. Abstract:

- Years of wars and economic sanctions were precursors to making the Iraqi monetary system captive to the wills of international parties, rather than to local necessities, forcing the Iraqi decision-maker to succumb to international dictates to maintain local stability.
- The postponement of closing the currency auction at the Central Bank, after the first few years of its opening due to a temporary circumstance, contributed to exacerbating the monetary crisis in Iraq. The purpose of societal stability was the driving force behind the opening of the currency auction, and it was imperative for the authorities to work on closing it to create a state of monetary cohesion in Iraq.
- Decisions by the US Treasury Department, along with international bodies' decisions, especially after 2003, strongly pressured towards reducing any chance of diversifying the national currency basket, leading Iraq to follow reactive policies in its monetary strategies.
- Sanctions affected 32 private banks in Iraq, constituting 43.2% of the total private banks in the country. The regulatory rules of the US Treasury Department allow for the removal of these banks from the sanctions list if they provide necessary information or follow the prescribed approach by the Treasury Department, placing the full

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responsibility on the Iraqi government to negotiate on behalf of the entities affected by sanctions.

- Tightening procedures, monitoring, and auditing of current banks, or those that may be established in the future, are necessary as reliance on electronic platforms for transaction verification and automatic stopping issued by these platforms is not sufficient. Many transactions cannot be discovered quickly enough, or there may be new and modern means of fraud against these platforms or the Central Bank, potentially leading to new problems for the Central Bank and Iraq. Prices are a reflection of market rumors, leading to sudden price increases as a result of any sanctions imposed on an Iraqi bank or company.
- Attempting to agree with countries that have trade relations with Iraq to use their local currencies to overcome the dollar shortage crisis, or to reduce pressure on the electronic platform, and limit the use and circulation of the dollar to countries with which there are no significant trade relations.
- Working steadfastly to fully and finally remove Iraq from Chapter VII and end the international and American guardianship controlling the country's fate.

## II. **Introduction**

The mechanism of economic sanctions is among the most effective mechanisms in our current time, due to its close connection with the economic, financial, and living situation of any country, as well as its direct and effective impact on the lives of citizens and meeting their basic needs and requirements across all aspects of existence.

The United States of America is one of the most important countries that adopted this mechanism and continues to do so today to regulate

and correct the actions and behaviors of countries to align with its aspirations and plans. Any country that deviates from what the United States has outlined for it, whether friend, ally, or foe, does not hesitate to use or actually use this effective and significantly influential means against it, in addition to imposing its dictates on it in a manner that ensures it does not undertake any act or behavior that could harm the decisions or interests of the United States wherever they may be on the global stage, due to its economic strength as the owner of the leading global currency, which is indispensable at present and in the near future at the very least, in addition to its largest economy, which constitutes 25.4% of the global economy, allowing it to exercise its dominance and strength amidst its political and military dominance alongside its economic infrastructure.

One of the most important measures taken by the United States as a form of sanctions is restricting access to the US dollar and exclusion from the global SWIFT system, as it did with Russia after the Ukraine crisis in 2022, leading to the collapse of the local currency due to its decreased real value and depreciation against the dollar, resulting in increased inflation rates as an inevitable outcome of this collapse, leading to a significant rise in prices for basic and luxury goods due to the currency's depreciation, resulting in a severe economic crisis, as seen in the Iranian case. This method is one of the most important means employed by the United States in pressuring countries, alongside freezing the targeted state's assets, causing it significant suffering in the face of these pressures.

When discussing the Iraqi case, the United States pressures Iraqi monetary and financial authorities to ensure the success of its policies in the region, especially the "maximum pressure" policy towards Iran and Syria, and preventing currency flow to these two countries to circumvent US sanctions against them. Due to Iraq's situation being linked to these countries alongside Turkey, the United States

exerts significant pressure to the extent of imposing sanctions on some Iraqi banks and companies to ensure the dollar does not flow from Iraq to these countries and to prevent the current Iraqi situation from being exploited for commercial activities that could help the targeted countries escape their predicament at Iraq's expense. Therefore, a set of measures (to be discussed later) were initiated to ensure the success of its policies. However, these measures have caused a significant crisis for Iraq, leading to a devaluation of its currency (the Iraqi dinar), which in turn has reflected on consumer price indices and other effects, signaling a potential economic disaster if the Iraqi monetary authorities (the Central Bank) do not adjust their stance and prevent the United States from imposing more extensive and significant sanctions than the current situation, which could lead to a major crisis.

### **III. Where did the American dominance over the Iraqi economic situation come from?**

After the American occupation of Iraq in April 2003, the US Treasury Department and the Coalition Provisional Authority sought to introduce a new currency as soon as possible to avoid inflation through exchange rate stabilization, and to establish the technical infrastructure and regulatory framework for the banking sector (interbank payments and currency auction sales). Initially, with the assistance of the United Nations, the US Treasury Department encouraged Iraq's international creditors to restructure the country's debt (approximately \$126 billion), and the US Treasury recovered the previous regime's frozen foreign assets, revenues from the "Oil for Food" program, and oil export revenues to establish the Iraq Development Fund in May 2003, dedicated to reconstruction. This fund is actually an account at the Federal Reserve Bank in New York, where dollars needed for restoring the infrastructure for oil and electricity, providing humanitarian aid, paying salaries of government employees, and establishing a national

budget by the Coalition Provisional Authority were transferred. The fund's name was later changed to the Iraq Development Fund, which today is used only for depositing Iraq's oil export revenues.<sup>1</sup>

In March 2004, the Coalition Provisional Authority enacted the Central Bank of Iraq Law No. 56 to grant it autonomy and ensure the bank would not use money printing to finance the state's budget deficit (as was the practice during the previous regime), thereby aiming to achieve two strategic objectives: curbing inflation and preventing a widespread popular uprising. In 2003, due to years of sanctions, the Iraqi economy was partially dollarized; due to a lack of confidence in the national currency, Iraqis relied on the dollar as much as they relied on the dinar for ongoing commercial transactions. The money supply in Iraq was determined by the stock of dollars and dinars, as well as by the exchange rate of the dinar against the dollar. In any economy that uses two currencies, the exchange rate has a significant impact on inflation rates. Individuals and investors prefer to have dollar reserves that they can use domestically and internationally, so even the slightest change in the exchange rate can lead to dangerous reactions, given that imported goods are purchased with dollars. Therefore, any change in the exchange rate can lead to hyperinflation. In Saddam Hussein's days, there was no official foreign exchange market, and dollars were sold by unofficial traders, creating a permanent state of uncertainty about the exchange rate, which varied significantly from one region to another.<sup>2</sup>

Since the overthrow of Saddam Hussein's regime in Iraq 21 years ago, the country's foreign currency reserves have been held at the American Federal Bank, giving the United States significant power to

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1. Dawood, Hashem. "On the Brink: The Strategic and Political Dimensions of the Dollar Exchange Rate Crisis Against the Dinar in Iraq." Emirates Policy Center, February 23, 2023. Web. Last visited February 24, 2024. <https://epc.ae/ar/details/featured/alabaad-alestiratijia-walsiyasia-li-azmat-sier-sarf-alduwlar-muqabil-aldynar-fi-aleiraq>.

2. Ibid.

control the supply of Iraqi dollars. To withdraw from these reserves, the Central Bank of Iraq requests dollars from the American Federal Bank, then sells the dollars at the official rate to commercial banks and exchange offices through a mechanism called the “currency auction,” which sells dollars for Iraqi dinars to help stabilize the local exchange rate and meet the population’s import needs.

Since then, Iraq’s oil revenues from selling oil go to the American Federal Bank after deducting 5% of those funds as compensation to the State of Kuwait, which was completed in recent years. Afterwards, it is transferred to the Central Bank of Iraq’s account after a request from the Iraqi Ministry of Finance, specifying where those funds will be spent. These requests are audited by the Federal Bank, and this process takes about 20 days. The funds are then transferred to the Central Bank of Iraq in Baghdad by planes carrying the money, with each plane carrying half a billion dollars, which incurs transportation, protection, and insurance costs paid by the Iraqi treasury.<sup>3</sup>

An account was opened at the Federal Reserve Bank in New York based on Security Council Resolution 1483 in 2003, issued after the fall of the previous regime in Iraq, which lifted the economic embargo on Iraq, returning it to its pre-1990 status. One of the paragraphs stipulates the creation of the Iraq Development Fund, which was granted international immunity to avoid seizure or confiscation as a result of international court decisions that could be issued based on claims against the previous regime.<sup>4</sup>

Initially, there were two funds: the Iraq Development Fund, which includes 95% of the oil revenues, and the Compensation Fund, which

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3. Al-Khalifa, Bilal. «The American Dominance over Iraqi Finance: The Role of the Federal Reserve Bank.» Draw Media Foundation, April 24, 2023. Web. Last accessed February 7, 2024. [https://drawmedia.net/ar/page\\_detail?smart-id=12672](https://drawmedia.net/ar/page_detail?smart-id=12672).

4. Ibid.



accounts for 5%, mostly going to Kuwait as many countries waived their debts except Kuwait. On June 15, 2003, Coalition Provisional Authority Director Paul Bremer issued Order 2, which deposited the funds of the Iraq Development Fund at the American Federal Bank in New York, directly managed by him alongside a manager appointed by the administration of the Central Bank of Iraq in cooperation with the American Federal Bank.

Following the security agreement named the Framework Agreement between Iraq and the United States of America, which led to the withdrawal of American forces from Iraq, officially ending the occupation of Iraq, a Security Council resolution 1956 was issued on December 15, 2010, in its 6450th session, ending the existence of the Iraq Development Fund at the request of the Iraqi government through a letter from Prime Minister Nouri al-Maliki, ending the oversight, immunity, and supervision over the Central Bank of Iraq. This agreement with the Federal Reserve was renewed to keep Iraqi funds with it, with the authority and management of these funds to be by the Central Bank of Iraq, but under the conditions and transparency of the American Federal Reserve.<sup>5</sup>

The Compensation Fund ended with the settlement of Iraq's debts to Kuwait, based on Security Council Resolution 687 under Chapter VII of the United Nations Charter in 1991. This occurred on December 23, 2021, when the last remaining payment of compensation to the State of Kuwait, amounting to 44 million dollars out of a total of 52.4 billion dollars, was made. Thus, Iraq, more than 31 years after its invasion of Kuwait, completed the payment of the full amount of compensations determined by the United Nations Compensation Commission under Security Council Resolution 687 of 1991. Specifically, on February 22, 2022, the Security Council in session 8972 took its decision number

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5. Ibid.

2621 to liquidate the Compensation Fund and close it, returning the remainder to Iraq and dissolving the Compensation Committee by the end of 2022, with its last meeting on December 9 of the same year. Following this, the compensation file was closed, and the oil resource was freed from this constraint. Therefore, it was no longer necessary to receive oil revenues in a single account neither in the Federal Reserve nor anywhere else.

These reserves provided the American administration with several advantages<sup>6</sup>:

1. The ability to pressure the government through its primary financial resource in shaping its budget and determining the exchange rate of the Iraqi dinar.
2. Control over the size and timing of funds exiting the American Federal Bank to Iraq.
3. Benefits accrued by American banks through borrowing Iraqi funds at very low interest rates, and the benefit of the companies transporting these funds from the United States to Iraq, including insurance and protection fees.
4. Maintaining the centrality of the dollar in the process of purchasing Iraqi oil, especially after the agreements made by China and other countries for currency swaps.

Therefore, this system (established under decrees issued by the Coalition Provisional Authority), fully supervised and guaranteed by the Federal Reserve in New York, is still in operation today. It functions as a tool to contain inflation, maintain confidence in the local financial system among investors and individuals, and prevent serious social unrest. It also aims to monitor any suspicious financial transfers and transactions and restrict them.

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6. Ibid.

#### IV. The Currency Auction and the Iraqi Monetary Situation:

The Central Bank of Iraq set a number of goals in establishing the currency auction, which dominated the dollar trade in the Iraqi market, as follows<sup>7</sup>:

1. A direct intervention tool to stabilize the value of the Iraqi dinar by defending an equilibrium exchange rate, which positively reflects on the general price level, especially for final imported goods and production inputs, and expands the export base.

2. A means to apply indirect monetary policy tools in managing the liquidity of the economy and controlling its levels, serving as a case of the practical application of the required open market operations in achieving balance in the monetary market and strengthening the chances of financial stability.

3. Financing private trade activity and their foreign currency trade exchanges, which previously depended on the parallel (black) market for financing needs, characterized by disorder and chaos in the 1990s. This led to an increase in the supply of goods covering the domestic demand for goods and products after the majority of government and private factories and plants stopped production, either due to destruction, power outages, or increased production costs, and opening borders for import and abolishing customs tariffs, which almost completely destroyed local production and its inability to compete.

4. The currency window was the main financier of the government in Iraqi dinars after converting its oil revenues obtained in dollars, which constitute more than 90% of the annual public revenues, and selling them to the Central Bank to be able to pay its operational and investment

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7. Al-Mashhadani, Abdul Rahman Najm. «Fluctuations in the Iraqi Dinar Exchange Rate in the Context of External Transfer Restrictions and the Possibility of Control.» Iraq Center for Futuristic Studies, Baghdad, February 22, 2023, pp. 2-3.

expenses in Iraqi dinars without the need to issue new currency, which could have increased the money supply and significantly contributed to limiting the growth of money supply.

5. Improving the purchasing power of those with limited incomes after the improvement of the dinar level and value against the dollar and its reflection on the real value of incomes.

6. Providing foreign currency resources at local banks for the purpose of enabling them to open documentary credits and letters of guarantee and conduct foreign currency transfer operations.

7. Opening investment horizons for the public (bank customers) for the purpose of developing their investments and economic projects and providing the necessary currency to finance the requirements of recreational, therapeutic, and educational tourism outside Iraq.

The currency auction was planned to continue for two or three years until the industrial and agricultural sectors were able to produce enough to meet the local market need. However, the auction has continued to this day, and its name has been changed to the currency sale window. The following table shows the sales of the Iraqi currency window.

Table 1. Total Annual Sales of the Currency Auction (in Billion Dollars).

Year	Cash sales	Cash transfers	Total sales
2014	14.6	37.2	54.5
2015	6	38.3	44.3
2016	4.7	28.8	33.5
2017	9.4	31.4	42.2
2018	8.8	38.3	47.1

Year	Cash sales	Cash transfers	Total sales
2019	5.8	45.3	51.1
2020	3.4	40.7	44.1
2021	6.6	30.5	37.1
2022	9.4	39.0	48.4

Source: Abdul Rahman Najm al-Mashhadani, “Fluctuations of the Iraqi Dinar Exchange Rate Under External Transfer Restrictions and the Possibility of Control,” Iraq Center for Futuristic Studies, Baghdad, 22/2/2023, pp. 2-3.

However, what happened was summarized by the current Prime Minister (Mohammed Shia’ al-Sudani), who confirmed the occurrence of “fraudulent dollar transfers abroad,” indicating that this was revealed by the beginning of applying regulations overseeing financial transfers. This step coincided with the decline in the dinar’s value against the dollar. The Iraqi dinar lost more than 10% of its value against the dollar within two months, leading to social unrest among the population due to the exchange rate’s deterioration.<sup>8</sup>

Al-Sudani, during a television interview with the official “Al-Ikhbariya” channel, mentioned that currency smuggling abroad was conducted through transfers based on inflated invoices for imports. He pointed out the existence of smuggling, saying, “Before the implementation of the (SWIFT) system, the Central Bank of Iraq sold traders amounts of green currency several times what it sells them today, yet there are no missing goods in the markets currently.” He added, “Previously, we used to sell 300 million dollars, 200 million dollars, 250 million dollars, in a single day. But now, the Central Bank sells daily 30, 40, or 50 million dollars, and what has changed? What is

8. «Prime Minister of an Arab Country Blames «Fraudulent Transfers» for the Dollar Crisis.» Al Arabiya News, February 1, 2023. Web. Last accessed February 23, 2024. <https://www.alarabiya.net/aswaq/economy/2023/02/01/أزمة-الدولار-في-الاحتياالية-التحويلات-باللوم-علي-التحويلات-الاحتياالية-في-أزمة-الدولار>.

missing in the market? Nothing.”<sup>9</sup>

Despite the currency auction functioning as an open market operation in exchanging dollars for Iraqi dinars to finance private sector foreign trade and a monetary policy for intervening in exchange rate stability and controlling local liquidity levels, it represents a form of financial corruption and a clear waste of financial resources. Dollar sales in the currency auction are divided into two parts; one related to amounts for remittance as support for banks abroad, which constituted 74.65% of total sales (2004–2020), and the other for cash dollar sales to banks and transfer companies within Iraq, which accounted for 25.35% of total sales during the same period. The pricing gap between the official dollar sale in the currency auction and the parallel market rate (2004–2020) peaked in 2012 and 2013, reaching values of 3,210.824 billion dinars and 3,513.246 billion dinars, respectively.<sup>10</sup>

It is concluded that financial waste and corruption were rampant in the Central Bank of Iraq’s auction, alongside the majority of hard currency leaking abroad in economic and financial activities fraught with a significant degree of fraud and money laundering. This led the American administration to take strict measures against the offending banks and companies involved in corruption and suspicious economic operations, which will be examined later.

## **V. Actions of American Financial and Monetary Authorities Against Iraqi Banks and Companies**

The American financial authorities, through the US Treasury Department, warned the Iraqi monetary authorities about violations, money laundering operations, and dealings with entities and individuals sanctioned by Iraqi banks and companies. Given the Central Bank of

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9. Ibid.

10. Shindi, Adeb Qasim. «The Impact of the Currency Auction on Financial Waste for the Period (2004–2020).» *Journal of Al-Kut College*, vol. 8, no. 2, January 2023, p. 230. Al-Kut, College Magazine. Top of Form

Iraq's lack of control over these matters, the US Treasury Department took several actions as follows:

1. Numerous currency exchange and currency trading companies were penalized, totaling 72 financial institutions during 2016 – 2017, and 4 money transfer companies were also penalized during the same years for reasons related to money laundering, manipulating currency sales and purchases, and smuggling it to neighboring countries of Iraq such as Iran, Syria, and Turkey.<sup>11</sup>

2. In November 2022, the Federal Reserve in New York began restricting the amount of dollars transferred to Iraq, complying with a policy the US Treasury Department had set years ago. In early 2020, the US Treasury Department asked the Iraqi government to comply with an electronic system that, according to American officials, aims to ensure the transparency of dollar transactions, combat money laundering, and stop the smuggling of dollars to Iran, Syria, and Turkey. These illegal activities are managed by banks and companies acting as commercial fronts, in addition to the physical transfer of dollars across borders. As a result of these restrictions, about 80% of dollar transfer requests in Iraq were rejected. It's noteworthy that since 2003, when Iraq's account was established at the Federal Reserve in New York, hundreds of millions of dollars were transferred daily to the Central Bank of Iraq, with an average of 250 million dollars a day in 2022, about 220 million dollars a day on January 15, 2023, and only 76 million dollars on February 9, 2023.<sup>12</sup> According to the old mechanism that was in operation for many years, the Central Bank and a special auditing company performed routine document audits and procedures followed by Iraqi banks participating in the currency sale window

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11. «The Central Bank Publishes Names of Banks Subject to U.S. Sanctions, According to Lists.» Al-Masra News, February 4, 2024. Web. Last accessed February 8, 2024. <https://almasra.iq/70261/>.  
Top of Form

12. Dawood, Hashem. Op. cit.

after executing financial exchanges, not before. This window is the institutional arrangement under the supervision of the Central Bank of Iraq in cooperation with the American Federal Reserve. Under this arrangement, these Iraqi banks could obtain US dollars after submitting requests containing necessary information regarding their purchases of products and goods requiring payment in dollars.<sup>13</sup> Based on these requests submitted through the Central Bank, these banks receive the requested dollar amounts from the Federal Reserve in exchange for an equivalent amount in Iraqi dinars. After these transfers, the Central Bank of Iraq and a specialized company routinely perform audits supposed to be thorough to verify the accuracy of the information provided by the participating banks, including purchase receipts. If these audits reveal errors and violations, the bank issues warnings, fines, or penalties to the offending banks, depending on the violation's magnitude and severity. In November 2022, after the United States required the use of an electronic platform for exchange operations, there was no longer a need for the previous auditing mechanism, as the platform now quickly examines the documents and information provided directly by the participating Iraqi banks, not through the Central Bank as before, accepting financial transactions that meet the required conditions and rejecting those with violations.<sup>14</sup>

3. Due to American conditions, the Central Bank shifted from the traditional cash transfer system (N22-O) to the electronic transfer system named (N2-2O-CO) using the electronic platform, also in response to the global financial transfer conditions (SWIFT), which requires the bank to fill out a form containing detailed information about the cash transfer operation accompanied by documents including the full name of the trader (transfer requester), the intermediary bank, the correspondent bank, the recipient of the cash transfer, full details about the type of goods (the purpose of the transfer), the port from

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13. Ibid.

14. Ibid. Top of Form



which the goods will be shipped, and the port through which the goods will enter Iraq. This, therefore, will be more accurate in monitoring transfer operations and their purposes, leading to a reduction in money laundering and smuggling activities. With the implementation of the electronic platform, the United States does not need to announce sanctions against banks; the platform itself “punishes” offending banks by depriving them of the ability to obtain US dollars, automatically preventing them through the platform itself. In usual contexts, the United States issues sanctions against banks through the US Treasury Department under specific charges such as supporting terrorism, money laundering, or transferring to entities under American sanctions like Iran and Russia, as happened in the case of the “Elaf Islamic Bank” in Iraq, which the Treasury placed under sanctions in 2012 for dealing with a sanctioned Iranian bank, with the Treasury lifting the sanction a year later following the bank’s compliance with US financial instructions.

4. The Central Bank of Iraq announced the punishment of 14 Iraqi banks and prohibited them from dealing in US dollars due to strong suspicions of smuggling dollars to Iran and Syria, under American economic and financial sanctions. The announcement of these “sanctions” did not come from an official American source nor the US Treasury Department or the Federal Reserve; nor were these sanctions announced on the official page of either institution. The announcement was made in a report by the American newspaper “The Wall Street Journal,” which attributed to unnamed American officials the decision by the Treasury Department and the Federal Reserve to ban 14 Iraqi banks from dollar transactions. Other English and Arabic news sources picked up the news from this American newspaper without relying on other official sources. This opened the door to further political confrontation between the United States and influential Shiite forces in Iraq, which are often accused of being behind the smuggling of dollars

to Iran using some banks as fronts (according to American data)<sup>15</sup>.

5. In January 2024, the Central Bank of Iraq decided to ban 8 local commercial banks from dealing in dollars, as part of measures taken to curb fraud, money laundering, and other illicit uses of the US currency, days after a visit by a senior official from the US Treasury Department to Baghdad. Following this decision, the eight banks were banned from participating in the daily dollar auction organized by the Central Bank of Iraq. The Central Bank of Iraq issued a document, verified by a bank official, listing the names of the banned banks, including Ashur International Bank, Investment Bank Of Iraq, Union Bank of Iraq, Kurdistan International Islamic Bank for Investment and Development, Al-Huda Bank, Al-Janoob Islamic Bank for Investment and Finance, Al Arabiya Islamic Bank, and Hammurabi Commercial Bank.<sup>16</sup> This brought the total number of banks that were penalized to 32 banks.

This awakening can be partly attributed to the geopolitical context in the region and the world, including the US administration's attempt to exert more pressure on Iran, which benefits most from the smuggling of dollars sold by the Central Bank of Iraq, along with Syria and Turkey. There's also the US desire to curb Russian and Chinese expansion in the Middle East and limit the effectiveness of any tripartite cooperation framework between Iran, Russia, and China, similar to the Comprehensive Strategic Partnership between China and Iran (March 2021), and the financial partnership between Russia and Iran outside the SWIFT system (January 2023), not to mention the growing concerns over tactics to circumvent sanctions against Tehran, Damascus, and Moscow. Parallel to the tightening monetary policy towards Iraq, the United States is exerting pressure on Turkey, which serves as the main hub for secret financial transfers for Iraq, Iran, and Russia.

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15. Abbas, Aqeel. «An Unintended Bubble: The Reality of American «Sanctions» on Iraqi Banks.» Emirates Policy Center, July 28, 2023. Web. Last accessed February 8, 2024. <https://epc.ae/ar/details/brief/haqiqat-alouqubat-alamrikiya-ala-almasarif-aleiraqia>. Top of Form

16. Ibid.

Undoubtedly, the measures taken by the Central Bank of Iraq in adopting the electronic platform for external transfers will limit suspicions of corruption and money laundering activities that accompanied the increase in currency window sales and their exploitation in the names of individuals unrelated to trade, where money is transferred in their names without their knowledge or through presenting forged documents as detailed in the documents. This coincides with the increase in cash transfers or cash sales conducted in the auction with the tax treasury theft scandal in 2022, which saw window sales reach record numbers never seen before in the auction.

However, the increase in window sales in 2022, along with the stolen tax treasury funds amounting to approximately \$2.5 billion, is noticeable. Sales of cash remittances for the months of December 2021 and from June to October 2022, which exceeded \$200 million daily on working days of the window from 2<sup>nd</sup> June 2022 to 25<sup>th</sup> October 2022 except for a few days close to it, peaked at \$248 million on 14<sup>th</sup> August 2022, coinciding with the increase in cash withdrawals for tax treasuries amounting to approximately \$522.6 million in local currency in June 2022. The table also shows a significant decrease in window sales from cash remittances to boost the balances of banks abroad after the decision to ban four banks from dealing in US dollars, which dominated a share estimated at 40–45% of daily window sales.

The increase in daily window sales, whether cash or remittances to boost the balances of banks abroad, indicates that exchange offices and banks exploit the window to pass suspicious funds, contributing to money laundering operations by presenting forged documents with fictitious names for transferring money outside Iraq in an official and legitimate manner. The old mechanism (N22-O) for operating the currency window facilitated the transfer and movement of money without precise supervision and full tracking from the trader in Iraq to

the final beneficiary, achieving the ultimate purpose of the transfer.<sup>17</sup>

## **VI. Monetary and Economic Effects of American Sanctions on Banks in Iraq**

The issue of the declining value of the Iraqi dinar against the US dollar is attributed not only to sanctions but also to the policy of the previous Iraqi government (led by Mustafā Al-Kadhimi) after it devalued the currency and raised the US dollar exchange rate according to its policy known as “the white paper.” The Central Bank of Iraq devalued the dinar against the US dollar in response to increasing economic pressures, including declining oil prices. The bank set the official exchange rate at 1460 dinars per dollar in 2020, instead of 1182 dinars per dollar, which had been the rate before that date, reducing the official currency value by about one-fifth. The Central Bank stated that this decision was made in light of the growing economic crisis and the challenges facing the Iraqi economy amid the ongoing COVID-19 pandemic. The bank added in a statement that policy failures dating back more than 15 years had exacerbated the crisis, emphasizing that the devaluation would be a one-time event and would not be repeated, aiming to support public finances and the requirements of public spending.<sup>18</sup>

The exchange rate reduction was the result of critical financial pressures, chosen for two reasons: first, to maximize the dollar revenues for the Ministry of Finance, considering it would sell the dollar at 1450 dinars instead of 1182 dinars, providing the Ministry of Finance with about 23% more revenue, over 20 trillion dinars, to bridge the deficit. The second reason was security for dollar sales, meaning when the dollar price rises to 1450, the Central Bank’s sales would decrease

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17. Al-Mashhadani, Abdul Rahman Najm. Op. cit., p. 4.

18. «The Iraqi Central Bank Reduces the Currency Value Against the Dollar by About One Fifth.» BBC News, December 19, 2020. Web. Last accessed February 4, 2024. <https://www.bbc.com/arabic/business-55379555>. Top of Form

compared to when the price is lower at 1182, due to the inverse relationship between the dollar price and the demanded quantity, at least for consumers. As the dollar price increases, the prices of dollar-denominated goods rise, which reduces demand and imports. Similarly, tourists' demand for dollars decreases when its price increases. These factors would lead to a decrease in demand for dollars, in addition to the frantic demand for dollars in 2020, resulting from real expectations of a currency devaluation due to increased dollar sales against decreased dollar revenues.<sup>19</sup>

However, exchange rate fluctuations significantly increased in the parallel market after the Federal Reserve's decision on 4<sup>th</sup> November 2022, to penalize four Iraqi banks from dealing in US dollars, accusing them of money laundering and transferring funds to entities and individuals on the US sanctions list: AlAnssari Islamic Bank for Investment and Financing, ALQabedh Islamic Bank Investment and Financing, Asia AlIraq Islamic Bank for Investment and Financing, and Iraqi Middle East Investment Bank, with the threat of penalizing other banks if they do not comply with external transfer mechanisms and conditions. Consequently, the Central Bank of Iraq decided to exclude these four banks from accessing the currency window and purchasing US dollars, allowing them to deal with other foreign currencies.

The dollar's price continued to rise in the Iraqi market, exceeding the 1650 Iraqi dinars mark by the end of December 2023, about 200 dinars above the official rate of 1450 dinars, leading to an increase in food and goods prices. This prompted the Iraqi government to take a series of measures to address the situation, including approving the dismissal of the Central Bank governor and appointing a new one. The crisis primarily resulted, as we will explain below, from the Federal Reserve's imposition of new stringent controls regarding the sale and

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19. «Economic and Social Implications of Re-changing the Exchange Rate.» Al-Furat Center for Development and Strategic Studies, March 26, 2022. Web. Last accessed February 4, 2024. <https://fcds.com/economical/1689>. Top of Form

transfer of dollars to Iraqi banks.

The Central Bank of Iraq, in a statement, indicated that the impact of US sanctions on the Iraqi economy is minimal, considering that the total assets held by the fourteen banks only constitute 1.29% of the total banking assets in Iraq. Moreover, the banks banned from transferring operations only constitute 8% of the total external transfers. The increase in the dollar exchange rate against the dinar is due to some dealers (traders) with the excluded banks turning to the parallel market and withdrawing large amounts of dollars to finance their commercial operations or to smuggle them abroad. However, the Central Bank of Iraq has imposed stricter controls on financial transfers in the country in general, while simultaneously ensuring the security and accuracy of transfer transactions.

According to the latest data, government banks, which do not exceed 7 banks, contributed 81.2% of the total credit provided to the central government, public institutions, and the private sector, compared to 18.8% contributed by the private banks operating in Iraq. Therefore, excluding these banks from dealing in dollars will have a very minimal impact on the Iraqi economy.<sup>20</sup>

Therefore, negotiations to resolve the crisis began with a meeting held in Istanbul on 3<sup>rd</sup> February 2023, between Brian Nelson, the US Treasury's Assistant Secretary for Terrorist Financing, and Ali Mohsen Al-Alaq, the governor of the Central Bank of Iraq. The meeting focused specifically on reforming the Iraqi banking sector and implementing anti-money laundering and counter-terrorism financing measures. The official statement released after the meeting pointed to a desire to achieve mutual goals through the application of anti-money laundering

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20. Al-Yasiri, Ibrahim Jasim. «The U.S. Sanctions on Iraqi Banks: Causes and Implications on the Iraqi Economy.» Akkad Center for Economic and Financial Studies, July 23, 2023. Web. Last accessed February 24, 2024. <https://acefs.org/archives/875>.

and counter-terrorism financing standards and the modernization of the Iraqi banking system.<sup>21</sup>

On 9<sup>th</sup> February 2023, Iraqi Foreign Minister Fuad Hussein met with his American counterpart, Antony Blinken, in Washington. No specific decision was announced following the meeting, but before it took place, Blinken emphasized that the United States was “now intensely focused on the economic dimension” of the strategic partnership framework agreement between the two countries. On 10<sup>th</sup> February, Wally Adeyemo, the Deputy Secretary of the Treasury, held discussions with Iraqi Foreign Minister Fuad Hussein and Central Bank Governor Ali Al-Alaq in Washington, focusing on anti-money laundering and counter-terrorism financing policies, but no specific resolutions for the meetings were disclosed. During his visit to Washington, Al-Alaq also met with Mahmoud Mohieldin, the Executive Director of the International Monetary Fund, who stated that the Fund is ready to assist in reforming the Iraqi banking sector.<sup>22</sup>

When the current budget law (2023–2025) set the official dollar rate at a threshold of 1,330 dinars, dollar exchange rates did not decrease but escalated. Rates in the parallel market reached 1,590 dinars per dollar due to merchants and companies avoiding the electronic platform to smuggle dollars out of the country, especially to Iran and Turkey. This created significant pressure on product prices and a substantial price increase, necessitating a stricter policy from the government and the Central Bank to control the exchange rate and prevent merchants from smuggling these funds out of the country.

Given the difficulty in controlling the parallel market, the crisis remains unresolved for the time being, alongside the United States hinting at more sanctions due to the current tense political and security

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21. Dawood, Hashem. Op. cit. Top of Form

22. Ibid.

situation. This is in addition to the activities of banks and exchange companies, which are surrounded by many suspicions of currency smuggling and dealings with entities under US sanctions, as well as money laundering and other charges presented by the US Treasury Department. Thus, the crisis continues until the economic and political situation in Iraq can be regulated.

## **VII. Conclusion:**

The management of the Central Bank and the American sanctions on Iraqi banks have created a significant crisis in the dollar exchange rate, which in turn has affected the consumer price index and inflation rates in the country, leading to a record surge in prices. Despite the solutions presented by the Central Bank and the Iraqi government to control the monetary situation and prevent the smuggling of Iraqi funds abroad and money laundering by private banks and money transfer companies, the situation has remained largely unchanged, signaling an economic crisis if the US Treasury Department were to execute its threats and prevent Iraqi banks and monetary authorities from accessing the dollars obtained from the sale of Iraqi oil, which are held in its accounts in the United States, thereby economically and financially strangling Iraq to an extent that could make the situation more severe than it was in Iraq before 2003, or in Iran currently due to the maximum pressure policy of 2018.

This American dominance over the Iraqi treasury, which amounts to approximately 115 billion dollars, along with its power to encircle the country through sanctions that have proven their strength and global impact, has significantly restricted the Iraqi authorities' movement and activity. Alongside the weakness of these authorities and their inability to curb the influence of neighboring countries and their significant manipulation of the currency market, both official and parallel, these



authorities are rendered incapable of performing their rightful role. Additionally, the political and economic weakness of some influential forces has rendered Iraqi financial and economic capabilities prey to them, allowing these forces to control and plunder without deterrence or fear of accountability or prosecution. Therefore, there is a significant fear that American financial authorities might punish the Iraqi people by imposing sanctions on institutions that cooperate with these political forces, overlook their actions, or even encompass government institutions entirely.

#### **VIII. Recommendations:**

A set of recommendations can be offered to overcome this crisis, as follows:

1. Tighten procedures, monitoring, and auditing of current banks or those that may be established in the future. Reliance solely on the electronic platform for transaction verification and automatic stoppage issued by this platform is insufficient, as many transactions cannot be detected quickly enough, or there might be new and modern methods of defrauding this platform or the Central Bank, potentially leading to new problems. As is known, prices reflect market rumors, leading to sudden price increases due to any sanctions directed at an Iraqi bank or company.
2. Attempt to agree with countries that have trade relations with Iraq to use their local currencies to overcome the dollar shortage or reduce pressure on the electronic platform, limiting dollar use and trading to countries with which we do not have significant trade relations. For example, imports from neighboring countries such as Turkey, Iran, and Saudi Arabia could be made in local currency. Considering that more than 50% of our commodity trade, especially food, means that more than 60% of traders' needs would decrease, reducing the impact

of the parallel market due to the diminished need to withdraw funds from it.

3. Expedite the process to completely and finally remove Iraq from the influence of Chapter VII, ending international and American guardianship that controls the country's fortunes to the extent that we expect severe sanctions due to any future crisis, as threatened by Donald Trump following the Iraqi parliament's decision to expel American forces from Iraq after the assassination of Abu Mahdi al-Muhandis and Qasem Soleimani. He stated that "we will punish Iraq to a degree that the sanctions on Iran will seem insignificant in comparison, and we will freeze all Iraqi funds," meaning sanctions may not be purely for economic reasons but any political disagreement with the ruling powers in Iraq could cost the people dearly.

4. Despite the shift to a digital system in financial transactions, which is a correct and efficient choice credited to the financial and monetary authorities, the slow implementation and errors in its application have significantly affected its correct implementation. Therefore, speeding up its full implementation across the country and overcoming current errors will lead to a better control of currency and funds circulation, enabling the government and the Central Bank to monitor suspicious activities like money laundering more effectively.