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Before the Senate Committee on Banking, Housing and Urban Affairs

**Sudan Divestment Issues:
The Darfur Accountability and Divestment Act
Wednesday, October 3, 2007**

Mr. Chairman and Members of the Committee, thank you for the opportunity to testify. My name is William Reinsch, and I am the President of the National Foreign Trade Council. Along with our USA*Engage coalition, we support multilateral cooperation and economic, humanitarian and diplomatic engagement as the most effective means of advancing U.S. foreign policy interests and American values. I am here today to express concern about the effectiveness and appropriateness of the sanctions measures under consideration with regard to Sudan.

There is no question that the situation in Sudan is tragic – or that United States and the international community must do much more to help. We are all horrified by the tragedy that has unfolded in Darfur, and we certainly respect the motivation of those who want to do something about it. But the challenge for Congress and the Administration is to pursue appropriate means that will actually effect change.

The problem with the approach passed by the House and now pending in your committee, H.R. 180, is that it is unlikely to have any effect. At the same time, its provisions pose serious foreign policy, Constitutional and compliance concerns.

Unilateral sanctions are rarely effective in achieving U.S. foreign policy goals. The Peterson Institute for International Economics has concluded that unilateral U.S. sanctions in place from 1970-2000 were effective only 19 percent of the time. Sanctions also provide a good excuse for the targeted government to blame its failures on outside pressures and to rally nationalist support for the regime.

Additional complications arise when the United States attempts to impose sanctions extraterritorially on companies established in other countries, particularly our allies. Those countries generally oppose such attempts and have enacted blocking statutes and other measures to counteract them. It also makes their cooperation with us on a multilateral approach much less likely.

Foreign policy measures by states and local governments are even less effective and infinitely more problematic. The governor and legislature of Texas, Illinois, or California are not the competent bodies to implement U.S. foreign policy, and their narrow divestment or procurement sanctions are unlikely to change the behavior of the target country. In addition, it baffles me why Members of Congress would want to take foreign policy out of their and the President's hands and subcontract it to local governments.

Sanctions by individual states also interfere with the President's ability to conduct foreign policy and impose enormous compliance difficulties for companies, as each state and local law is different from the others, creating as many as 50 different foreign policies, each with different rules and different lists of sanctioned companies.

State measures also impose compliance costs on businesses. A company could be on a divestment list in New Jersey but not in California, which will put mutual funds in an impossible position, being told to divest to comply with legal requirements in one state but having a fiduciary duty in other states not to do so. In addition, there are costs to companies and investors in having to monitor, research, and comply with the various laws, which may differ from federal policy, as well as having to pay the fees they incur when they sell stocks pursuant to a divestment requirement and then buy new ones. In Illinois, the combined lists of so-called "forbidden entities" doing business in Sudan named 233 companies. Had it not been declared unconstitutional, the law would have affected 581 vendors of investment products, and a screening of Morningstar's database suggested at the time that over 900 equity mutual funds owned at least one forbidden entity.

Neither is divestment free for retirees. In addition to transaction costs, divestment increases the risk to shareholders by limiting the pool of stocks and funds. One consequence of the initial Illinois divestment law, for example, was that many of the small, highly-regulated pension funds likely would have had to move out of international mutual funds and into bond funds, at the time cutting their annual rate of return by almost half.

Most important, we believe foreign policy sanctions enacted by state governments are unconstitutional. In 2000, in *Crosby v. NFTC* the Supreme Court struck down Massachusetts' Burma sanctions on the ground that they violated the supremacy clause of the Constitution. The Court declared, "It is simply implausible that Congress would have gone to such lengths to empower the President if it had been willing to compromise his effectiveness by deference to every provision of state statute or local ordinance that might, if enforced, blunt the consequences of discretionary Presidential action."

The Darfur Accountability and Divestment Act

With respect to H.R. 180, I first want to commend Adam Sterling and the Sudan Divestment Task Force for their work in crafting principles governing their divestment efforts. Their ideas have shaped this particular piece of legislation for the better. I also want to thank your staff, Mr. Chairman, and Senator Shelby's staff for their hard work in trying to develop a workable bill. Unfortunately, serious problems remain.

First, divestment and procurement bans are likely to face challenges at the World Trade Organization by our trading partners, who will see their extraterritoriality as a violation of our trade commitments. Japan and the European Union brought a WTO case against the Massachusetts sanctions on Burma, which was mooted by the Supreme Court's decision in Crosby.

Second, the bill fails to limit state divestment measures and thus gives the states inappropriate leeway that interferes with the President's ability to conduct foreign policy. For example, Section 4 of H.R. 180 authorizes divestment for entities that appear on "any list developed by the State or local government for the purpose of divestment from certain persons." Allowing such alternate lists increases the likelihood of divergent state laws, reduces transparency, and has the effect of contracting out our foreign policy to private list-preparing entities which often have financial interests or their own foreign policy agendas. In addition, it appears that the state and local government lists authorized by the bill are neither limited to the sectors specified for the federal list nor provide the same exemptions. That would mean, for example, that states could require divestment from a company operating in southern Sudan pursuant to an OFAC license.

Third, there are parts of the bill where further clarification is needed. For example, in Section 2, using proprietary information to develop a public list poses serious transparency issues, as investors and targets of the list may not be able to access the data to determine why or how an entity was included. The very idea of a public list is also problematic, since it is often difficult to distinguish with certainty actual business conducted from meaningless press conferences held to tout a memorandum of understanding that is never acted upon. For example, the SEC's attempt to develop a list proved to be a complete disaster. In addition, the safe harbor provisions of Sections 6 and 7 appear to apply to divestment and procurement pursuant to the federal list but not to lists developed by individual States.

Finally, and of great importance, the authorization for States to enact procurement bans in Section 9 directly contradicts the Supreme Court's decision in the Crosby case. In that case, the Court made abundantly clear that the supremacy clause protects the flexibility required for the Executive to conduct a coherent foreign policy. Divergent state foreign policy sanctions constrain that. The Court wrote, "Quite simply, if the Massachusetts law is enforceable the President has less to offer and less economic and diplomatic leverage as a consequence." Furthermore, the Court found that state sanctions [quote] "compromise the very capacity of the President to speak for the nation with one voice in dealing with other governments."

Beyond these specific concerns, there is the slippery slope problem. If Congress encourages states to act on a particular foreign policy issue through H.R. 180 or other similar legislation, it will surely tempt them to pass similar divestment and procurement legislation affecting other foreign policy issues.

The Sudan Divestment Task Force has done an admirable job in attempting to establish a targeted divestment model. They are making a good faith attempt to target their efforts specifically at Sudan and to avoid divestment in other situations, but theirs is not the only effort and genocide in Sudan is not the only cause. There are other blanket divestment movements

gaining momentum in state legislatures that would target companies doing business in Iran, and other countries, including China.

If the Committee nonetheless decides to act favorably on H.R. 180, it would be better policy if it included a clear statement of policy in the bill which would expressly limit the ability of states to impose foreign policy sanctions. Congress should take this opportunity to discourage divestment in any circumstances except those specifically authorized by the Congress in H.R. 180 or subsequent legislation. By doing so, Congress would preserve the primacy of the federal government in making foreign policy and help ensure uniformity in state and local government actions.

Nevertheless, I would also urge the Committee to take a step back and reevaluate the impact of this legislation versus its potential costs. There are more effective ways to help the people of Sudan. Organizations like Save Darfur and ENOUGH support a range of other approaches, which are truly multilateral and which might actually have some effect, including fully funding a hybrid Africa Union-UN force focused on civilian protection and urging the Administration to make peace in Darfur a higher priority in its international diplomacy. Likewise, the call by Senators Biden and Lugar for further support for peacekeeping, high-level diplomatic talks, and further multilateral sanctions to bind Khartoum's commitments is a welcome development.

These measures – which would bring the force of the international community to bear on the conflict in Sudan – are more appropriate ways to work towards achieving the outcome that we all desire.