Stopping Iran's Nuclear Ambitions

THE CA$E FOR TARGETED SANCTIONS

AMERICAN JEWISH COMMITTEE

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Iran presents a clear and present danger to international peace and security. Its ambitions to become the dominant power in the region, its heavy-handed interference in the domestic affairs of its neighbors, its lavish support for terrorist groups, and its massive arms build-up all underscore the nature of the threat. Moreover, in its quest to pursue nuclear weapons, Iran has been found in violation of the Nuclear Non-Proliferation Treaty (NPT) and UN Security Council resolutions. Finally, Iranian leaders have called for a world without Israel.

Iran's nuclear weapons program is particularly worrisome. Experts believe that the regime is developing ballistic missiles to deliver nuclear weapons, could transfer weapons of mass destruction to its terrorist proxies for delivery, and could wield its nuclear deterrent as political blackmail throughout the Middle East. In light of these scenarios, the international community has turned to economic penalties to demonstrate to Iran's policymakers that a nuclear-armed Iran is unacceptable.

Because Iran's economy is integrally linked to the global market, economic sanctions have been presented as a possible means to influence the regime and persuade it that there will be a painful price for flouting the will of the international community. With the implementation of sanctions and the threat of further ones, Mahmoud Ahmadinejad, the president of Iran, has increasingly become a target of criticism from legislators. The conservative media that represent the views of Supreme Leader Ayatollah Ali Khamenei called on the Iranian president to stop provoking the U.S.; and in elections last December for Tehran's city council, Ahmadinejad's slate was widely defeated. These developments suggest that Iranian elites do not necessarily approve of the regime's agenda, and that sanctions may have more direct impact than skeptics believed.

Despite Iran's destabilizing influence in the international arena, investors from around the world continue to supply vast sums of money that not only prop up the regime, but also serve to embolden it. What follows is a review of some notable measures being used in an attempt to change Iranian behavior, an analysis of Iran's international trade links, and a sampling of additional economic and political measures available to the international community to demonstrate its displeasure with Iranian behavior.

In response to the seizure of the U.S. embassy in Tehran by radical students, the Carter administration enacted significant sanctions against Iran beginning in 1979. Since that time, several other sanctions measures have been put in place through acts of Congress and executive orders by the president. Below is a selection of the U.S. sanctions to date.

1979: **Executive Order 12170** (President Jimmy Carter)

- Freezes all Iranian assets held within the U.S.

1995: **Executive Order 12957** (President Bill Clinton)

- Bans U.S. investment in Iran's energy sector

1995: **Executive Order 12959** (President Bill Clinton)

- Bans most U.S. trade with Iran

1996: **Iran Sanctions Act** (formerly the Iran-Libya Sanctions Act)

- Requires the president to impose sanctions on non-U.S. companies investing more than $20 million annually in Iran's energy sector

2005: **Executive Order 13382** (President George W. Bush)

- Names fourteen individuals and entities associated with Iran's weapons of mass destruction and missile programs, denies them access to the U.S. financial system, and freezes their assets in U.S. banks

2006: **Iran Freedom Support Act**

- Extends the Iran Sanctions Act to 2011
- Codifies many of the sanctions that were set out in previous executive orders

A 1979 image of U.S. hostages being marched in Tehran by their radical student captors. Photo courtesy of Corbis.

The International Community's Actions—UN Sanctions

Despite concerted international efforts, the Iranian government has continued to develop its nuclear program, has withheld information from the International Atomic Energy Agency (IAEA), and has been found in non-compliance with the NPT. As a result, the IAEA referred the Iranian nuclear issue to the UN Security Council, which has the power to adopt binding and enforceable resolutions, including resolutions that provide for sanctions. Thus far, the Security Council has adopted three resolutions under Chapter VII of the UN Charter addressing the Iranian nuclear threat, with a fourth resolution currently under discussion.

The Security Council voted in favor of Resolution 1696 in July 2006, giving Iran one month to suspend its enrichment-related and reprocessing activities, including research and development. When the IAEA found that Iran did not comply, the Security Council passed Resolution 1737 in December 2006.

December 2006: **UN Security Council Resolution 1737**

- Freezes assets of ten firms and twelve individuals tied to Iran's nuclear and missile sectors
- Prohibits sale to Iran—or financing of such sale—of technology that could contribute to Iran's uranium enrichment or heavy-water reprocessing activities

March 2007: **UN Security Council Resolution 1747**

- Freezes assets of an additional thirteen organizations and fifteen Iranian citizens involved in Iran's nuclear programs, missile development efforts, and the Revolutionary Guard (the military branch responsible for Iran's ballistic missiles)
- Bans the sale or transfer of Iranian weapons to any nation or organization

The International Community's Actions—The EU's Mixed Message

In addition to America's broad sanctions regime and the introduction of UN sanctions, the EU—Iran's largest trading bloc—has begun to implement its own restrictions on dealings with Iran. At the same time, however, a number of EU member states continue to extend generous export credit guarantees and, in some cases, maintain robust economic ties with Iran.

EU Sanctions

The EU, on April 22, 2007, exceeded UN requirements by imposing a full arms embargo on Iran and expanding the list of people considered *persona non grata,* subject to a travel ban and an assets freeze.

Credit Guarantees

Export credit guarantees are government-backed credits that cover both commercial and political risk to encourage trade with target countries. Germany, Austria, Italy, and France, among others, all provide government-backed export guarantees to Iran. In 2005, the EU member states supplied an estimated $22 billion in guarantees for trade with Iran.[1] While this figure reportedly decreased to $18 billion in 2006, there is obviously much more that could be done.[2]

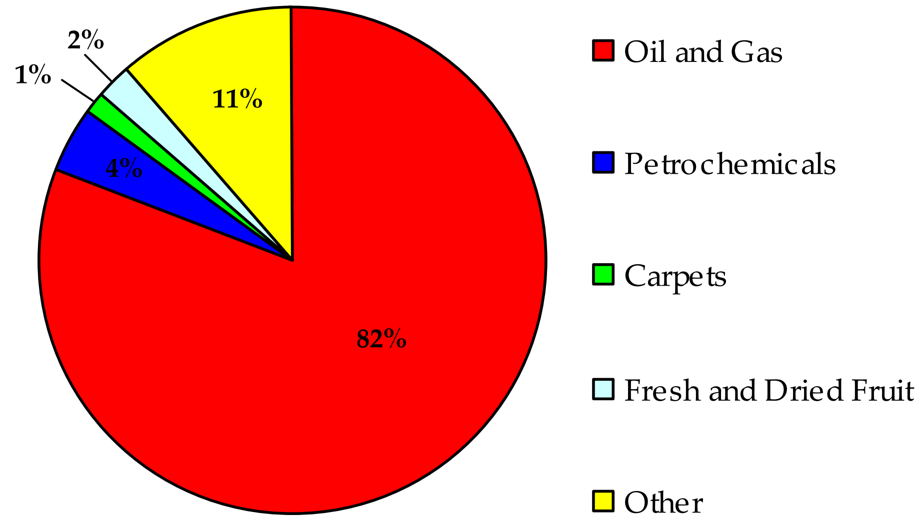
Iran's primary exports are unrefined oil and gas, which together account for over 80 percent of foreign earnings and 50-60 percent of the government budget.[3]

Top Destinations of Iranian Exports (2005/2006*)[4]

1.	Japan	($59.6 billion)
2.	China	($10.1 billion)
3.	Turkey	($7.12 billion)
4.	South Korea	($3.48 billion)
5.	Italy	($3.34 billion)
6.	Netherlands	($2.89 billion)
7.	France	($2.50 billion)
8.	Taiwan	($2.38 billion)
9.	South Africa	($2.38 billion)
10.	Greece	($1.91 billion)

* 12-month fiscal period, ending March 20, 2006

Exports by Sector (estimated figure, 2006)[5]



Trade with Iran—Iranian Exports

Many foreign companies have entered Iran to capitalize on the country's oil and gas reserves. Iran benefits from their presence through profit-sharing, tax revenue, and increased political clout, to name but a few.

Some of the major energy companies that have invested at least $20 million in a given year in Iran are shown below on the right. Below, to the left, are three examples of recent major deals:

Total, **Gazprom**, and **Petronas**, in 1997, agreed to a $2 billion deal to develop South Pars. South Pars is estimated to hold half of Iran's total gas reserves.[6]

In January 2007, **Repsol**, in partnership with **Shell**, signed a preliminary deal worth approximately $4.3 billion to further develop South Pars.[7]

Total, along with **ENI** and **Bow Valley Energy Ltd.**, invested approximately $300 million to develop Iran's Balal oil field.[8]

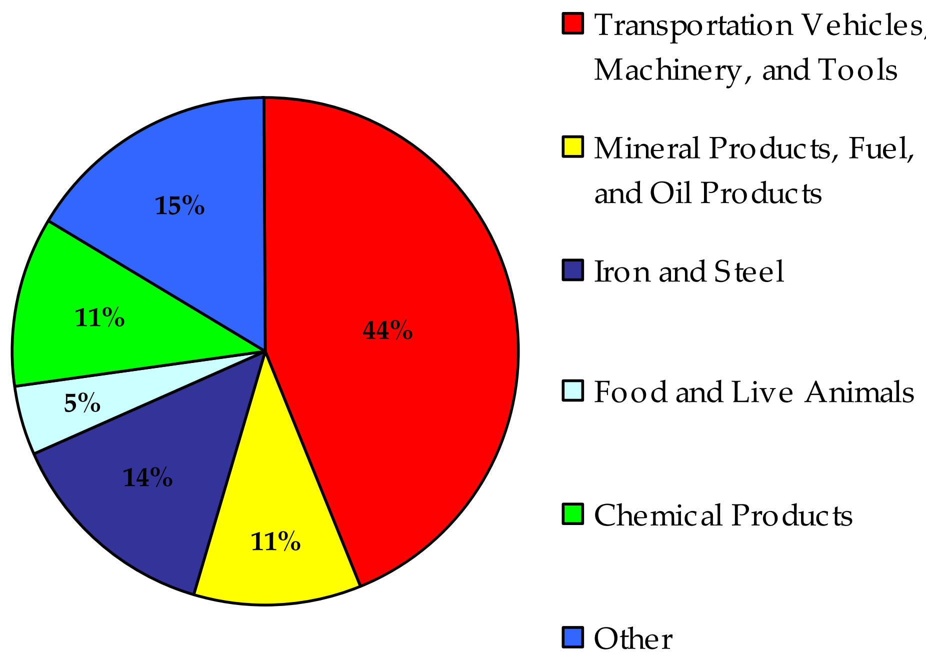
The Swiss energy group **EGL** arranged for the supply of 5.5 billion cubic meters of gas from Iran to Europe over the next 25 years. The deal's estimated value is reportedly between 10 to 22 billion euros.[9]

While Iran has the third largest known oil reserves, it does not have sufficient refining capacity for its domestic consumption. The United Arab Emirates, the largest exporter to Iran, and other countries refine the oil for Iranian use. Iran is also unable to domestically produce heavy machinery and cars. Instead, it imports these products, principally from Europe and Asia.

Top Nations Providing Imports to Iran (2005/2006*)[10]

1.	UAE	($7.67 billion)
2.	Germany**	($5.15 billion)
3.	France	($2.65 billion)
4.	Italy	($2.36 billion)
5.	China	($2.16 billion)
6.	South Korea	($2.10 billion)
7.	Japan	($1.31 billion)
8.	Switzerland	($1.27 billion)
9.	India	($1.11 billion)
10.	Russia	($1.03 billion)

Imports by Sector (2005/2006)[11]



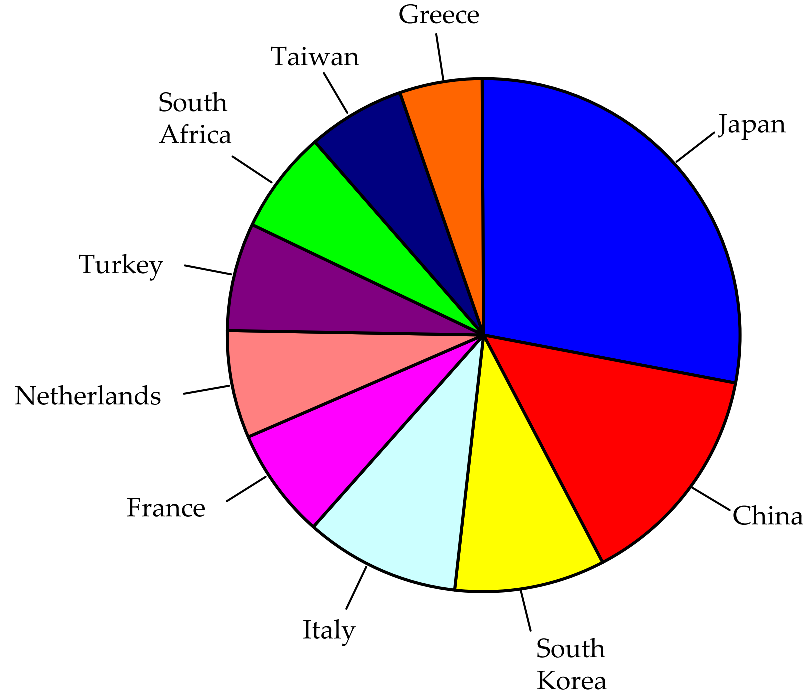
*12-month fiscal period, ending March 20, 2006.

** Germany supplies Iran with much of the country's heavy machinery and motor vehicle parts. German companies doing major business include, but are not limited to, Siemens, BASF, and Daimler-Chrysler. (Source: AJC-Business Relations with Iran)

Oil and gas represent 80 percent of Iran's exports. The leading destinations are Japan and China, which buy over one-third of Iran's estimated 2.5 million barrels per day (b/d) of oil exports.[12]

Top Destinations of Iranian Crude Oil
(b/d, 2006)[13]

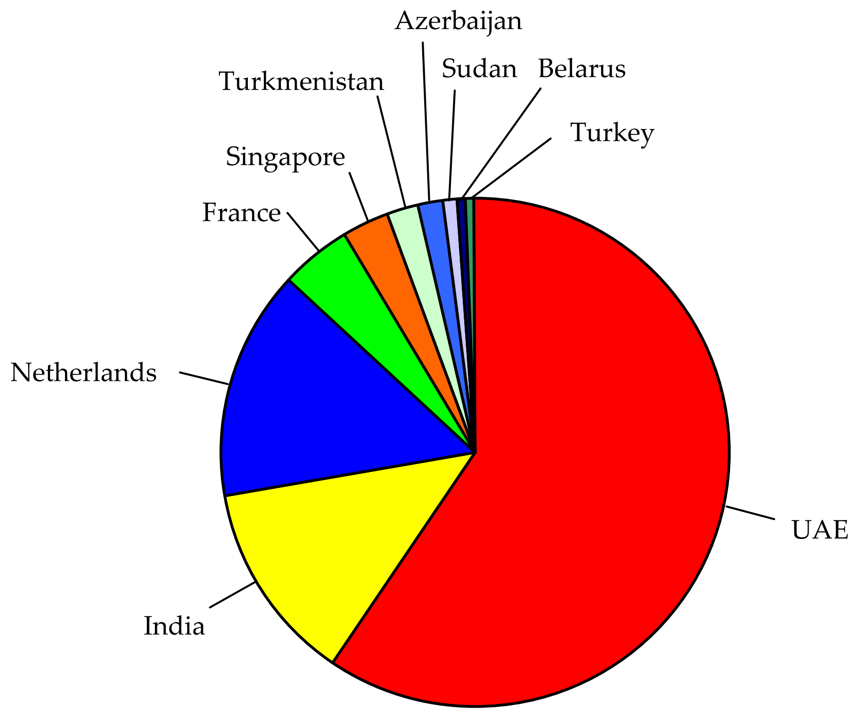
1	Japan	(570,604)
2.	China	(284,830)
3.	South Korea	(195,654)
4.	Italy	(193,935)
5.	France	(142,811)
6.	Netherlands	(139,246)
7.	Turkey	(138,873)
8.	South Africa	(134,646)
9.	Taiwan	(125,031)
10.	Greece	(105,236)



Because of Iran's lack of refining capacity, it relies on foreign countries to provide as much as 40 percent of its domestically consumed gasoline.

Top Suppliers of Gasoline to Iran[14]

1.	UAE*	($2.57 billion)
2.	India	($558 million)
3.	Netherlands	($363 million)
4.	France	($197 million)
5.	Singapore	($127 million)
6.	Turkmenistan	($91.0 million)
7.	Azerbaijan	($68.2 million)
8.	Sudan	($31.8 million)
9.	Belarus	($30.1 million)
10.	Turkey	($21.5 million)



* The UAE serves as a major transshipment point for regional and European gasoline headed to Iran.

Trade with Iran—The Banking Factor

European banks facilitate billions of dollar- or euro-denominated transactions with Iran, including in the energy sector. The U.S. Treasury Department has led a global effort to convince financial institutions and the nations that regulate them of the "reputational risk" associated with doing business in Iran. As a result, several European banks have ended or curtailed activities there.

Some major financial institutions active in Iran

In 2003, Belgium's **Fortis** led a banking consortium that arranged for a $370 million deal to build a steel plant in Iran.[15]

In 2004, **Deutsche Bank** of Germany arranged a $1.75 billion loan to National Iranian Oil to develop the South Pars gas field.[16]

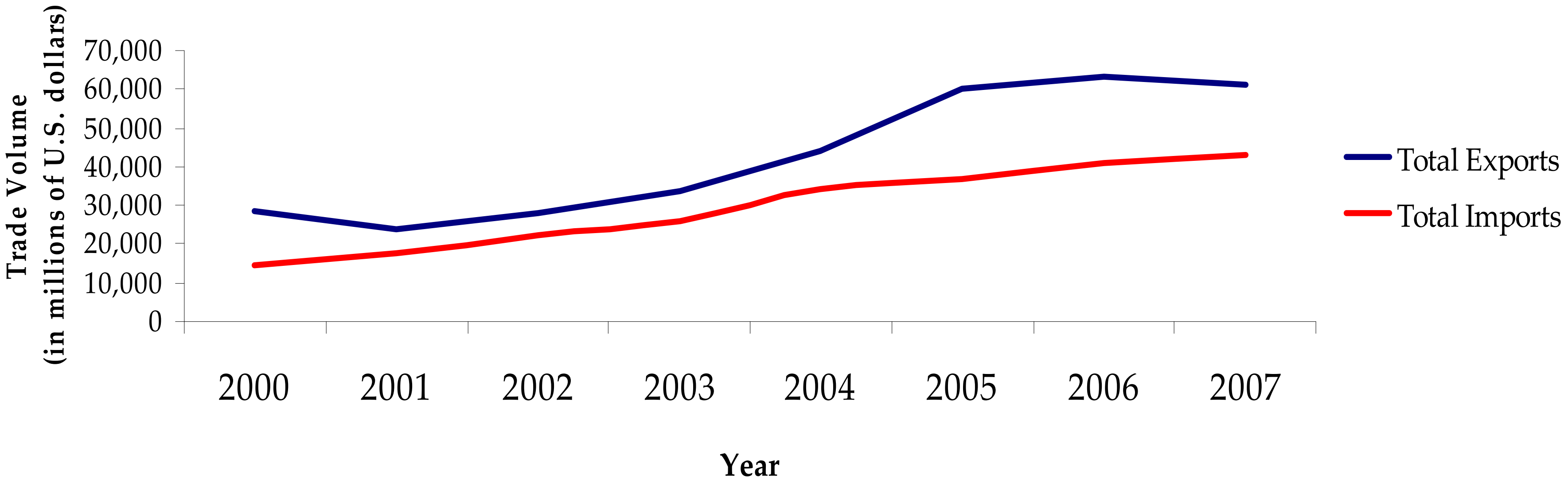
Also in 2004, France's **BNP Paribas** participated in a consortium that agreed to loan Iran $180 million for the construction of a power plant.[17]

Major financial institutions that have ceased or curtailed activities in Iran

Switzerland's **Credit Suisse** and **UBS** said they would stop all new business with Iran.[18] Germany's **Commerzbank**,[19] France's **Credit Lyonnais** and **Societe Generale SA**, Britain's **HSBC** and **Barclays PLC**, and Holland's **ABN Amro** have announced curbs on dealings with Iranian banks and businesses.[20]

Trade with Iran has increased over time and, barring steps to curtail it, volume is expected to continue to increase in the future.

International Trade with Iran[21]



Because of Iran's highly integrated economy, the international community has the potential ability to greatly influence Iran's decision-making and direction. There has been much discussion about incentives and disincentives to affect Iran's behavior. Here below are some of the most oft-discussed "carrots" and "sticks."

Economic and Political "Carrots"

The following are economic and political incentives for Iran, first offered by the Permanent Five Members of the Security Council and Germany in June 2006. While the offer was rejected, the package remains on the table.

- Direct U.S. participation in negotiations
- Lifting of U.S. sanctions, allowing Iran to buy spare parts for Boeing aircraft
- Light-water nuclear reactors
- U.S. and EU backing for World Trade Organization (WTO) membership

Economic and Political "Sticks" (Sanctions)

- Ban foreign investment in Iran's energy sector
- Restrict the sale of equipment and technology to Iran for oil and gas exploration, production, refining and transportation
- Pressure key suppliers of gasoline to limit their exports to Iran
- Divest from companies investing in Iran
- Eliminate export credit guarantees
- Ban travel and freeze assets of Iranian officials involved in nuclear and ballistic missile programs
- Embargo arms sales to Iran
- Downgrade diplomatic relations with Iran
- Limit participation of Iranian teams in international sporting events

As concern over Iran's nuclear program grows, government and private sector divestment campaigns in the U.S. are emerging. Federal and state legislation, for example, aims to screen public investment funds for holdings in companies doing business in Iran's oil sector.

State Divestment Legislation Currently under Consideration

California

Florida (passed, May 2007)

Georgia

Illinois

Louisiana

Missouri

New Jersey

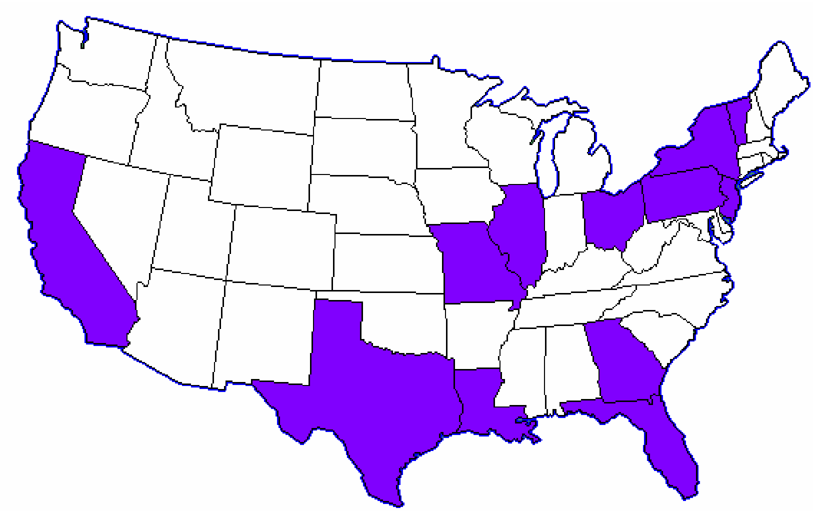
New York

Ohio

Pennsylvania

Texas

Vermont



Federal Divestment Legislation Currently under Consideration

Iran Sanctions Enabling Act (2007)

"Targeted financial measures represent one of the strongest non-military tools available to convince Tehran that it can no longer afford to engage in dangerous, destabilizing activities such as its nuclear weapons program and its support for terrorism."[22]

-- Excerpt from the pending Iran Sanctions Enabling Act

- Requires U.S. government to publish a list of companies investing more than $20 million in Iran's energy sector
- Authorizes state and local governments to divest the assets of their public investment funds from any company on the list
- Protects fund managers who divest from companies on this list from lawsuits by investors who are unhappy with the results

As this publication details, the international community has a wide array of economic measures available to it to seek to dissuade Iran from pursuing its nuclear ambitions. Iran's dependence on the international community for capital and markets offers the best chance to influence its behavior. Those countries with a financial stake in Iran have the ability to demonstrate, tangibly, that they will not do business with Iran at any cost. Unlike North Korea, under severe sanctions and dependent on the outside world for providing for its people's most basic needs, Iran maintains lucrative links with the outside world that, directly or indirectly, serve to strengthen the regime.

Faced with stepped-up economic pressure, Iran might be compelled to reconsider its present course of action. Its heavy reliance on the energy sector—accounting for up to 60 percent of the government's budget—offers the most obvious area where additional measures could pack a powerful punch. By introducing tougher sanctions, the international community could conceivably change the regime's cost-benefit analysis of pursuing nuclear weapons. The object, it should be stressed, is not to target the Iranian people, but its government's policies.

Iran presents nations of goodwill with arguably the most pressing geostrategic challenge today. Will the international community take the admittedly risky, but ultimately necessary, diplomatic and political steps to prevent Iran from realizing its nuclear intentions? Or will it allow other diplomatic, political, or economic concerns to prevail?

No nation should relish the idea of military confrontation any more than it should relish the prospect of Iranian nuclear weapons. If there is a third way, and we earnestly hope there is, then this report may offer some helpful guidance.

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