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**COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN  
PARLIAMENT AND THE COUNCIL**

**EU RELATIONS WITH THE ISLAMIC REPUBLIC OF IRAN**

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## EU RELATIONS WITH THE ISLAMIC REPUBLIC OF IRAN

### 1. BACKGROUND

#### Relations with the EU and Member States

At present the EU does not have any contractual relations with Iran, nor is there any significant financial co-operation. An Agreement existed in the time of the Shah, but it lapsed in 1977 before the Islamic Revolution. An EU-Iran dialogue was initiated in 1995. After the election of President Khatami in 1997 this was extended to new areas and became the Comprehensive Dialogue in 1998. A dialogue meeting is held every six months in Troika format.

The Comprehensive Dialogue allows a wide ranging exchange of views on :

- *global issues* (terrorism, human rights and proliferation),
- *regional issues* (Iraq, Gulf, Central Asia, the Middle East Peace Process)
- *areas of cooperation* (drugs, refugees, energy, trade and investment).

The Comprehensive Dialogue has contributed to improving relations but it is clearly limited in scope. It has been complemented by a number of technical working groups between the Commission and Iran, which have served to identify areas of mutual interest and possible co-operation (see section 4 below). However, it is clear that the lack of a contractual framework limits the development of such co-operation.

Relations with Member States have improved considerably since President Khatami was elected in 1997. The Italian Prime Minister visited Teheran in 1997. In 1999, President Khatami visited Italy and France, and the Presidents of Austria and Greece visited Iran in the same year. President Khatami recently visited Germany. Numerous visits by Foreign Ministers and other Ministers have taken place. British-Iranian relations were unblocked in 1998 by the defusing of the Rushdie *fatwa* issue and Ambassadors were exchanged in mid-1999.

Iran has manifested a strong interest in strengthening relations with the EU, and has shown interest in negotiating a Trade and Co-operation Agreement and an enhanced relationship with the EU is clearly a major policy objective for President Khatami.

## **Relations with other countries**

Since the US Embassy hostage crisis of 1980/1981 the US has followed a policy of containment of Iran. It has applied a range of sanctions - most recently the February 2000 Iran Non-Proliferation Act. US policy towards Iran, which is largely driven by Congress, is slowly evolving. However, despite recent statements from former Secretary of State Albright, further rapprochement between the US and Iran will await events and the new US Administration. Meanwhile the US wants the EU to maintain pressure on Iran, especially over issues such as human rights, weapons of mass destruction and alleged state-sponsored terrorism. Views on Iran are exchanged twice a year in the EU Troika-US-Canada trilateral talks.

### **2. THE CURRENT SITUATION IN IRAN**

Democratic municipal elections were held in Iran in February 1999 and Parliamentary elections took place between February and April 2000, both elections resulting in victory for reformers. The next Presidential elections are scheduled to take place in June 2001.

Iranian politics are characterised by a constant power struggle between the reformers and two major groups:

- The Conservative centres of power (Council of Guardians, Assembly of Experts, Militant Clergy Association etc.) under the final authority of the Ayatollah Khomeini, keep control of much of the judiciary, revolutionary armed and security forces and are able, and continue, to obstruct reforms. They have reacted to the results of the parliamentary elections by widespread closure of the reformist press and by arresting a number of reformist figures;
- The minority "Islamic Right" with only 50 - 60 out of 290 seats in the Majles, draws its support largely from the Bazar merchants and shopkeepers, the revolutionary Guards and militias, certain Foundations and the judiciary. It is now on the defensive.

President Khatami has succeeded in allowing the majority of the Iranian electorate to express its wish for change through the democratic process. It is clear from these elections that a large majority of voters (particularly women, students, secular urban and rural populations) seek civil, political and economic reform in Iran. While President Khatami has no intention of threatening the foundations of the Islamic Republic, nor challenging the unelected theocratic post of the Supreme Guide, he recognises the groundswell of dissatisfaction with the arid politics of the Conservatives. President Khatami and the Reformist movement will continue to pursue a peaceful civil and economic evolution within the existing political framework of the Islamic Republic. In this the Reformers will have some tacit support from the more pragmatic hardliners, including the Supreme Guide, who have recognised where their longer term interests lie. Nonetheless, the evolutionary process will be slow and difficult.

While the democratising process of President Khatami has allowed reformers to take the high ground both in the legislature and in the executive (the previous Majles was dominated by hard-liners), it remains for the reformers to prove that they can implement President Khatami's programme of economic, civil and legal reform. Ayatollah Khamenei's instruction to the Majles not to debate the proposed Press Reform Bill is the most important setback but there have been positive signs in other areas of reform.

In the field of human rights, the 2000 UNCHR Resolution sponsored by the EU notes and confirms that considerable improvements in Human Rights have been recorded in Iran, although much still remains to be done.

The trial of 13 Jews in Shiraz as well as the trial of the intellectuals participating in the Berlin Conference are severe embarrassments for President Khatami and the reformers. The sentences in both trials were harder than anticipated. Regarding the Shiraz trial, the EU has formally expressed its regret and its hope that the convicted will be pardoned. A similar EU Declaration has been made expressing deep concern about the harsh verdicts in the Berlin Conference trial and the hope that the appeals procedure will lead to acquittal.

In other areas, the EU has also expressed its concern, e.g. the death sentences passed on the student rioters (July 1999 riots) and, at the same time, the acquittal or very light sentences passed on the police officers responsible for provoking the students.

In the field of press freedom, matters have deteriorated in the last few months; the previous (conservative) Parliament (Majles) succeeded in adopting a more restrictive press law before elections in February, since when more than 20 reformist journals and magazines have been closed and their editors put on trial or indicted. Ayatollah Khamenei's later intervention forbidding the new Majles to debate a Press Bill was an unexpected setback to the reform movement. Nonetheless, new journals which support reform are beginning to appear.

President Khatami has indicated that press freedom and the reform of the judiciary are high on his Government's list of priorities and to be tackled as soon as possible. In both cases the challenge is considerable; the judiciary under Ayatollah Al-Hashini Shahrudi remains for the time being a formidable instrument of the conservatives.

Despite the mixed picture described above, the prospects for positive and gradual political evolution in Iran are better than they have been since 1979. Despite some recent setbacks, the reformists are likely to be able to consolidate their position on the basis of the broad and unambiguous support they received in the February elections.

### **3. TRADE AND ECONOMY**

The population of Iran is about 65 million and is growing fast. GNP is about € 180 billion. The economy is inefficient, unreformed and centralised. In order to improve its economic performance in the long term, Iran needs to move towards a market economy and to open up to the rest of the world. A reforming Five Year Plan was introduced at the end of 1999 and even though it was diluted by the old Majles, it remains the main instrument for reforming the economy. Despite the currently high price for oil Iran faces a difficult economic situation and needs to accelerate the pace of reform.

Iran has the second largest gas reserves in the world (16% of total world reserves), third largest oil reserves (10%) and straddles a most vital geo-strategic position.

The EU is Iran's largest trading partner ( $\pm$  40% of total Iranian imports). EU exports to Iran have varied between € 3.5 – 5.0 billion since 1995 and are dominated by manufactured goods, vehicles, chemicals and pharmaceuticals.

Iran's exports to the EU ( $\pm$  36% of total Iranian exports) have ranged between € 3.7 – 5.7 billion (Iran controls imports through licensing, so the balance of payments is in its favour). Exports to the EU are dominated by petroleum ( $\pm$  80% of total), followed by carpets, pistachios and caviar.

Iran's external debt, including rescheduling undertaken 1996-9, now amounts to \$10 billion and has fallen in recent years.

The World Bank has recently made two loans amounting to \$ 230 million for water and sewerage projects and the IMF maintains normal relations and is ready to assist with any macro-economic stabilisation programme.

The level of EU trade with Iran is far from being in line with the potential of this country in terms of population and natural resources. Many difficulties for importers and investors remain - some improvements have been announced but not yet implemented. The administrative and legal environment for trade and investment is, according to the representations of the Member States in Teheran, intransparent and arbitrary and therefore discouraging for importers and potential investors. Difficulties have been reported, for example, with regard to the treatment of the expatriate personnel of foreign companies, the granting of import licences, foreign ownership and the repatriation of profits.

### **4. EC-IRAN COOPERATION**

In October 1998, the Council asked the Commission to establish contacts with Iran to explore possibilities for cooperation. A Commission-Iran Technical Meeting was organised in December 1998 and it was agreed to explore a number of *possible* areas for co-operation – energy, environment, transport, agriculture, drugs control, refugees and human rights. With the exception of some humanitarian assistance and limited aid for drugs control,

there is at present no EC-Iran financial and technical cooperation. In some areas working groups have been set up between the Commission and the Iranian administration.

- Current engagements

Working Group on Energy -	met in Teheran, May 1999 ; A Synergy project will be finished in February and a second meeting of the Working Group organised in Brussels in March 2001
Experts Meeting on Drugs -	first meeting in December 1999 ; small project financed; two others being examined now (Council Reg. No. 2046/97)
Experts Meeting on Refugees -	meeting in April on Afghan and Iraqi refugees; ongoing projects with UNHCR and NGOs, more examined (Council Reg. No. 443/97), also by ECHO
Working Group on Trade and Investment -	first meeting in Teheran on 28-29 November 2000

Following the Energy working group meeting in 1999, Iran has become a observer of the Commission funded INOGATE programme, and has the possibility of becoming a full member. In addition, Iran is an observer in the Tacis funded TRACECA-east-west land communication programme. In its recently adopted Green Paper on the security of energy supply (COM(2000)/769), the Commission stresses the need to establish an on-going dialogue with energy producing countries in order to increase market transparency and price stability. EU energy discussions with Iran take place in the framework of the Producer-Consumer Dialogue.

To date, it has not been possible to undertake discussion in the other areas listed above although there are some actions relating to human rights which could be developed in the future.

## 5. EU INTERESTS

The EU has both political and economic reasons to develop closer ties with Iran. Increased democracy and greater respect for human rights would contribute to making Iran a more stable partner in the region. Iran is an important source of petroleum and gas in a strategic location with its own strong interests in adjacent areas, e.g. in Central Asia. Iran could in future

have a significant potential as a regional economic partner, offering substantial opportunities for trade and investment. However, this potential will only develop if Iran engages in a major overhaul of its trade and economic policies.

Drug trafficking through Iran from Afghanistan and beyond has a direct impact not only on Iran but also on Europe, and Iran carries a heavy burden in the fight against the traffic. In addition, Iran shelters a disproportionate number of refugees (1.9 million), in particular from Afghanistan and Iraq. The combination of a growing refugee fatigue in Iran together with the continued instability of neighbouring countries risk possible further negative developments in Iran itself.

Under the right circumstances the development of closer EU-Iran relations could help to promote the reform process in Iran and contribute to greater regional stability. Iran has indicated that it is ready to discuss human rights, which is a positive sign since any future contractual relations with Iran would have to include discussion on human rights issues. In addition, Iran is also ready to discuss security issues, including regional security, and has begun to do so with some Member States.

## **6. CHALLENGES TO CO-OPERATION**

A number of issues need to be addressed, bilaterally by the EU and Iran and unilaterally by Iran if co-operation is to be deepened and extended to new areas. These concern both political and economic issues. On the political side, these include:

### **Human Rights**

Although Iran has made positive changes in recent years, its human rights record still gives cause for concern (on issues such as the position of women, allegations on the use of torture, persecution of certain minorities, suppression of press freedom etc.). As part of developing closer relations the EU and Iran should engage in regular dialogue on these issues.

### **Support for radical groups**

The US and Israel regularly charge Iran with hostile rhetoric with respect to the Middle East Peace Process as well as with giving support to extremist groups, in particular certain Palestinian groups such as Hamas and Islamic Jihad, and its support to the Hizbollah in Lebanon has never been hidden. Some of the rhetoric is indeed unhelpful and Iran has made it clear that it does not have confidence in the Peace Process.

In the early 1990s, both former President Rafsanjani and the Supreme Guide Khamenei declared that Iran had ceased to export its revolution; President Khatami has confirmed a more reconciliatory foreign policy and Iranian sponsored terrorism in the EU seems to have ceased since 1995.

It should be noted that Iran itself claims to be a victim of terrorism. This relates in particular to the Mojahedin-e-Khalq; based in Iraq whence attacks are regularly launched on Iranian targets, but there has also been criticism of European countries harbouring radical opposition groups.

### **Security Issues**

Iran's intention to develop weapons of mass destruction, and in particular long-range missiles, is a matter of serious EU concern. The EU encourages Iran to conclude a strengthened safeguards regime with the IAEA. Iran has repeatedly stated that the conclusion of such a regime, like its possible willingness to ratify the Comprehensive Test Ban Treaty (CTBT), should depend on prior removal of international export control measures against its civilian nuclear programme. The EU does not accept such precondition.

All the above areas of concern are raised in the Comprehensive Dialogue.

### **Economic Reform Issues**

On the economic side, any strengthening of trade and economic co-operation between the EU and Iran will be conditional on Iran pursuing a policy of economic liberalisation, which is a necessary pre-condition if the country is to attract significant investment flows.

## **7. ASSESSMENT AND RECOMMENDATIONS**

Provided that the reform process continues, it is clear from the preceding analysis that it is in the mutual interest of the EU and Iran to develop closer ties, politically and economically, as well as in areas like environment, drugs and migration. Given the possibilities of unforeseen reverses in Iran's own political evolution and its weak economic structures, a cautious approach is required and in view of the number of areas which give rise to concern the development of closer relations should be gradual and dependent on progress made by Iran in these areas. The Commission and the Council should regularly review progress in the light of indicators or benchmarks in areas such as the rule of law, rights of minorities, press freedom, the regulatory environment for the economy and Iran's approach to foreign relations and security matters.

In the light of the analysis set out above and the conclusions of the General Affairs Council of 20 November 2000, the Commission recommends to the Council to develop closer relations with Iran on the basis of the following approach. It goes without saying that the scope for promoting bilateral relations will depend on the progress of political, economic and legislative reform in Iran.

- encouragement of political and economic reform through
  - more frequent official and unofficial bilateral contracts



- development of exchange/co-operation in areas of mutual interest and concern (such as drugs, rule of law, refugees etc)
- readiness to engage in dialogue on human rights
- strengthening the CFSP dialogue by deepening the dialogue in areas such as regional security, weapons of mass destruction , nuclear proliferation)
- seeking appropriate ways of developing people to people contacts
- promotion of bilateral economic relations through
  - negotiation of a Trade and Co-operation Agreement.
  - continuation of Commission – Iran working groups on energy, trade and investment.

The Commission recommends the continuation of the dialogue on Iran with other partners;

If these recommendations are accepted by the Council, the Commission will consider presenting to the Council, in accordance with Article 300(1) of the Treaty, a recommendation to be authorised to open the necessary negotiations.