



Testimony of William A. Reinsch
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Before the Senate Committee on Finance

S. 970, "The Iran Counter-Proliferation Act of 2007"
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Mr. Chairman and Members of the Committee, thank you for the opportunity to testify today. My name is William Reinsch, and I am the President of the National Foreign Trade Council. Along with our USA*Engage coalition, my organization supports economic, humanitarian and diplomatic engagement and multilateral cooperation as the most effective means of advancing U.S. foreign policy interests and American values. I am here today to express serious concern about the approach to sanctions contained in S. 970, the Iran Counter-proliferation Act.

There is no question that Iran's behavior poses grave concerns for the United States and our allies. Iran's pursuit of a nuclear program is deeply troubling, and its documented support for terrorist organizations is unacceptable. These are serious problems that require the sustained attention and involvement of the United States.

But it is important to consider which approach is most likely to change the behavior we all want to see changed. By picking fights with our allies and limiting the ability of this and future Presidents to negotiate directly with Iran, legislation like S. 970 would make it more difficult for the United States to address the threats posed by Iran.

Members of this Committee, as well as the Committee on Banking, Housing and Urban Affairs, must balance the need to stand strong against Iran's unacceptable behavior against the risk of doing something counterproductive in an effort to address it. Passing S. 970 would come at a heavy price.

Unilateral sanctions will not change the equation

As a general matter, unilateral sanctions rarely achieve 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, and most successes came where a modest policy change – like release of a political prisoner – was sought. Moreover, sanctions may make the problems they are intended to address worse by providing an excuse for the targeted government to blame its failures on outside pressures and to rally support for its regime.

In the case of Iran, our ability to change behavior through future sanctions is further limited because the United States already maintains comprehensive restrictions on trade. Given that the regime has learned how to survive through decades of sanctions, more pressure by the United States alone is very unlikely to convince Iran to change its behavior.

Instead, the best hope of altering Iran's behavior is through vigorous and unified multilateral pressure in concert with our allies and Security Council partners, combined with direct diplomacy with Iran.

Unfortunately S. 970 – and other legislation such as HR 1400, which has been referred to the Banking Committee – would make it more difficult to unify our partners behind further multilateral measures and would also impede efforts by this and future Presidents to conduct direct diplomacy with Iran.

S. 970 would endanger multilateral diplomacy

Section 8 of S. 970 would expand current unilateral U.S. sanctions to foreign companies by making a parent company liable for the actions of its foreign subsidiaries. This bill would draw international attention away from the core problem: Iran's threatening behavior in seeking nuclear weapons. Instead, the bill would effectively penalize entities and individuals in the very countries whose cooperation we need to effectively counteract Iran's behavior. These other governments could draw on already-existing blocking statutes (e.g. the EU) or implement new measures to counteract the threat of U.S. penalties.

If enacted, this provision would over-ride and preempt provisions of the 17 Executive Orders issued over a 28 year period that provide legal authority for the current sanctions. This effort is a dramatic departure from current policy. The last time the United States attempted to sanction foreign companies in this way, in the 1980s, it caused a major rift with our allies, leading President Reagan to halt his initial attempt. The simple fact is extraterritorial sanctions are more likely to cause a trade war than they are to change Iran's behavior.

Adequate authority exists in current U.S. law for the United States Government to target sham corporations that exist to circumvent domestic sanctions. Simply put, if a subsidiary is independent and legitimate, it should not and cannot be held to U.S. law for conduct that remains outside the United States. If it is not independent and legitimate, then the U.S. government already has adequate enforcement authority.

S. 970 would limit U.S. diplomatic efforts with Iran

S. 970 would also limit the ability of the President to conduct diplomacy. Section 7 of the bill would codify existing Executive Order prohibitions on all exports except those of food and medicine to Iran and would prohibit the import from Iran of any good. Codifying these prohibitions would remove the ability of a U.S. President to offer incentives or to respond to positive developments in Iran in a timely fashion. For example, in the 1990s, the United States allowed imports of caviar and rugs in response to what was perceived then as a political opening in Tehran. It is essential that future Presidents have the same tools available to them, even if there are no present plans to employ them.

In addition, the prohibition on U.S. exports would appear to disallow transactions that are encouraged under current law. Under the current wording, this provision would seem to prohibit the export of medical devices to Iran and could hinder the ability for NGOs or news organizations to operate in Iran.

This approach presents a number of humanitarian concerns

I want to speak briefly about how this legislation could affect the people of Iran. As noted, Section 7 (b)(2) would prohibit all exports to Iran except for food and medicine. Banning the export of medical devices to Iran could compromise the basic medical treatment of Iranian citizens. It also seems unwise from a humanitarian standpoint to prohibit the export of civil aviation parts, which are currently permitted under license because they are directly related to air safety. Further, this provision could inhibit the ability for NGOs, international organizations such as the United Nations and news bureaus of the U.S. press from working on humanitarian activities.

In a broader sense, sanctions often end up hurting ordinary people while having little impact on the government leaders we are trying to influence. In the case of Sudan, poorly drafted state laws have discouraged American business activity in southern Sudan at the same time the federal government is trying to encourage it. In the case of Cuba, dissidents like Oswaldo Paya oppose U.S. economic sanctions because they provide an excuse for the Cuban government's failings.

These are just some of the problems with S. 970. USA*Engage has compiled a list of concerns with the legislation, which are attached to my testimony and which I would ask be submitted for the record.

Diplomacy and multilateral pressure are better approaches

We believe that the best way to change Iran's unacceptable behavior is through an approach that emphasizes multilateral pressure and direct talks with Iran. The United States should continue to work with the UN Security Council on ways to pressure Iran on its nuclear program and with our allies around the world to confront its support for terrorist activities.

The Congress should also consider endorsing and funding a high-level special envoy for Iran with the authority to engage in direct bilateral talks in partnership with the international community. The United States has made some progress negotiating an end to North Korea's nuclear weapons program through direct diplomatic engagement. When it comes to Iran, there is already a framework for cooperation – security talks in Baghdad – and precedent – the United States and Iran cooperated in the past to support democratic governance in Afghanistan.

In addition, the Treasury Department has also been successful in convincing European banks to curb their dealings with Iran. This type of back-channel economic diplomacy with our allies is a much more effective way to influence the behavior of foreign companies than the sledgehammer approach of S. 970.

Finally, despite your best efforts, I will guarantee you that if S. 970 is enacted it will have serious unintended consequences which will be manifested rather quickly, and which would make our efforts to change Iran's behavior significantly more difficult. I strongly urge the Committee to reject this approach and instead to endorse diplomatic efforts with our allies and with Iran that are much more likely to result in a positive outcome.

Comments on Specific Provisions of S. 970

Section 5 would make the United States more vulnerable to international commercial complaints and damage U.S. global financial leadership by greatly expanding the universe of entities subject to sanctions to include insurers, creditors and foreign subsidiaries. The United States would undoubtedly face complaints and lawsuits from our trading partners questioning their legality if sanctions were imposed on these entities.

Section 6, Russia Nuclear Cooperation could undermine U.S. multilateral efforts to stop Iran from developing nuclear weapons -- for which Russia's cooperation is indispensable. The Bush administration's decision to negotiate a Section 123 agreement with Russia was reached based on the fact that Russia had already taken important steps to prevent Iranian proliferation. These steps included Russia's insistence that Iran return all plutonium-laden spent fuel from the Bushehr reactor to Russia and Moscow's support for three UN Security Council resolutions sanctioning Iran's nuclear activities. Indeed, President Bush supported Russia's provision of nuclear fuel to Bushehr on the basis that guaranteed fuel supplies undermine Iran's assertion of the need to enrich its own uranium.

A Section 123 Agreement provides the legal basis for the U.S. to enter into nuclear cooperation with another country and outlines the terms and conditions for cooperation. It does not comprise a commercial contract and does not relieve a country of the need to obtain U.S. export licenses for equipment, material, and technologies. Such an agreement does not remove continuing leverage over our nuclear partners, both through licensing and possible legislation.

The United States should certainly seek greater Russian cooperation on Iran, but S.970 is counterproductive in terms of achieving that cooperation. The most likely outcome of this provision would be to weaken Russia's willingness to cooperate with the United States in blocking Iranian nuclear efforts.

There are also other advantages to allowing a US-Russian 123 Agreement to enter into force. Nonproliferation experts have noted that a 123 Agreement between the U.S. and Russia could yield important nonproliferation benefits such as providing the international community with greater access to Russia's civil nuclear facilities. A 123 Agreement could also lead to increased efforts to secure and dismantle Soviet-era nuclear weapons. A 123 Agreement could also open tech transfer in critical areas from Russia to the United States and encourage Russia's Participation in the U.S. led Global Nuclear Energy Partnership (GNEP). Such an agreement could be important in its own right.

Section 7 (b)(1), Prohibition on Imports – would prohibit the import from Iran of any good. Codifying these prohibitions would remove the ability of a U.S. President to offer incentives or to respond to positive developments in Iran. For example, in the 1990s under the leadership of President Bill Clinton and Secretary of State Madeline Albright, the United States allowed the import of caviar and rugs in response to what was perceived then as a political opening in Tehran. It is essential to provide those same tools to future U.S. Presidents, even if there are no present plans to employ them.

Section 7 (b)(2), Prohibition on Exports – While the prohibition here is not as explicit as it is in Section 203 of HR 1400, it is clear that this would prohibit export of civil aviation parts, which is

a matter of air safety. If American companies can provide civil aircraft parts that would prevent an Iranian airliner from going down over Iran – or, for that matter, over Europe – it is reasonable to allow such sales to take place. In addition, the prohibition on U.S. exports would seem to disallow transactions that are encouraged under current law. Current wording would seem to prohibit the export of medical devices to Iran and could hinder the ability for NGOs or news organizations to operate in Iran.

Section 7(b)(3), Accession to the WTO orders USTR to take no action that would extend preferential trade treatment or lead to accession to the WTO of a country “engaged in nuclear cooperation with Iran.” Russia’s accession to the WTO would be tremendously beneficial for the United States and the global trading system. It is the largest economy outside of the WTO and is an important market for a range of U.S. industry from manufacturing to agriculture. Welcoming Russia into the WTO would level the playing field for American workers and businesses, and would allow us to compete on more equal footing with local and foreign firms. Holding up this unrelated and beneficial economic process is inappropriate.

Section 8 proposes that the existing unilateral U.S. prohibitions of trade and investment with Iran by U.S. persons and entities be expanded to apply to certain overseas entities and citizens of other countries by making the parent company liable for the actions of its subsidiaries that are domiciled in foreign countries. If enacted, this provision would over-ride and preempt provisions of the 17 Executive Orders issued over a 28 year period that provide the legal authority for the current sanctions. This effort is a dramatic departure from current policy, which is an outgrowth of past experience.

During the Soviet invasion of Afghanistan in the early 1980s, the U.S. sought to ban participation in the Siberian pipeline project by European subsidiaries of U.S. companies. In response to the U.S. sanctions on the pipeline project, the U.K., France, and other countries passed blocking statutes, requiring the subsidiaries to honor existing contracts and disobey the U.S. sanctions, thereby putting the subsidiaries and their parents in the impossible position of not being able to obey both U.S. and applicable foreign law at the same time.

Under considerable pressure from European governments and American corporations, the Reagan Administration withdrew the extraterritorial measures to avert adverse rulings in multiple pending legal cases in both U.S. and overseas courts. Beginning with the regulations implementing sanctions on Libya in 1986, the U.S. has repeatedly limited investment and trade prohibitions to U.S. based companies.

In targeting our allies for penalties, this bill would draw international attention away from the core problem: Iran’s threatening behavior in seeking nuclear weapons. Instead, the bill would penalize entities and individuals in the very countries whose cooperation we need to effectively counteract Iran’s dangerous behavior. These other governments could draw on already-existing blocking statutes (e.g. the EU) or implement new measures to counteract the threat of U.S. penalties.

At the same time, adequate authority exists through existing U.S. law for the United States Government to target phony or sham corporations that exist to circumvent domestic sanctions. U.S. law already sets parameters to determine the nature of a subsidiary and its relationship to its parent. If U.S. companies are operating sham foreign subsidiaries, then the U.S. government

already has authority to investigate and prosecute such cases and enforce current regulations. Simply put, if a subsidiary is independent and legitimate, it should not and cannot be held to U.S. law. If it is not independent and legitimate, then the U.S. government already has adequate enforcement authority. S. 970 would establish overreaching extraterritorial legal definitions for international business relationships and complicate legitimate trade and investment and reigniting the firestorm that ensued in the Siberian gas pipeline case.

Section 10: would reduce U.S. contributions to the World Bank proportional to the amount the Bank provides for projects in Iran. Such a move would damage U.S. credibility within the institution and across the multilateral institutions, which would undermine our broader development agenda. It is important for the U.S. to live up to its multilateral obligations.