

Congressional Testimony

**Testimony by Mark Dubowitz, Esq.
Executive Director
The Foundation for Defense of Democracies
Director, the Iran Energy Project**

**Hearing before the House Committee on
Oversight and Government Reform
Regarding the Implementation of Iran Sanctions**

**Washington, DC
July 29, 2010**



1726 M Street NW • Suite 750 • Washington, DC 20036

Introduction

Thank you, Chairman Towns, Ranking Member Issa, and members of this distinguished committee for the opportunity to testify. I am honored to appear before you today. In my testimony, I will examine the efficacy of energy sanctions and how they can encourage the leaders of Iran to abandon their unlawful nuclear program, their training and financial support for international terrorist organizations, and their repression of their domestic political opponents.

The *Comprehensive Iran Sanctions Accountability and Divestment Act* (the “*Comprehensive Act*”) that President Obama has just signed into law gives him more authority (when combined with existing executive orders and legislation) than any U.S. president has ever had to counter the Iranian threat. Like his predecessors, President Obama has repeatedly said that preventing Iran from acquiring a nuclear weapon is a top priority. If that is the case, the Obama administration can strike a blow at the heart of Iran’s energy business, without which Tehran would face significant economic and political challenges.

If sanctions were sufficiently severe, Iran’s leaders might decide that nuclear weapons were not worth pursuing. And if these sanctions yielded no compromise, no one could argue that America and its allies had ignored peaceful options to prevent Iran from developing nuclear weapons.

The Impact of Sanctions on Iran, and How Tehran is Skirting Them

Oil provides the Iranian government with the majority of its revenues. Iran also has the second largest natural gas reserves in the world after Russia, which could give Tehran even more influence over global energy markets if it acquires the requisite investment and technology.¹ Yet, in spite of the country’s enormous oil and gas reserves, Iran’s energy infrastructure is rusting. The *Wall Street Journal* recently noted that “Iran’s beleaguered oil industry could be on its way to passing an ignominious milestone: being replaced [by 2015] by its onetime nemesis, Iraq, as the Middle East’s second-biggest oil producer.”²

During President Mahmoud Ahmadinejad’s first four years in office, foreign investment in Iran’s energy industry plummeted by 64 percent, from \$4.2 billion to \$1.5 billion.³ Government mismanagement has also hamstrung Iran’s energy sector. Ahmadinejad has replaced a number of competent energy technocrats with regime loyalists, including Revolutionary Guard officials who had no previous experience in the energy business.

¹ U.S. Energy Information Administration, “Iran,” *Country Analysis Briefs*, January 2010, p. 8. (<http://www.eia.doe.gov/emeu/cabs/Iran/pdf.pdf>)

² Spencer Swartz and Benoit Faucon, “Iran’s Falling Oil Output Means Less Revenue, Clout,” *The Wall Street Journal*, June 26, 2010. (<http://online.wsj.com/article/SB10001424052748704569204575328851816763476.html>)

³ Doron Peskin, “Iran: Foreign Investment in Oil Drops During Ahmadinejad’s Term,” *Ynet News*, April 30, 2010. (<http://www.ynetnews.com/articles/0,7340,L-3880348,00.html>)

Iranian officials now say that without an annual investment of at least \$25 billion, Iran could become a net importer of oil.⁴

As a result of its limited refining capacity and domestic subsidies, which have driven up demand for gasoline, Iran already imports approximately 30 percent of its gasoline from foreign suppliers. For the U.S. and its allies, this presents a significant opportunity to increase pressure on the regime.

According to a 2009 Congressional Research Service report, the mere threat of sanctions has “constrained Iran’s energy sector significantly.”⁵ Not only are Iran’s gasoline suppliers exiting the market, but energy investors, banks, technology providers, and insurers now face growing pressure to choose between doing business with the Iranian regime and continuing their business relationships in the far larger U.S. market.

The recently-passed U.S. energy sanctions are now complemented by U.N., E.U. and Canadian actions. In June 2010, the United Nations Security Council took critical first steps to target the Iranian energy sector. The preamble of the recently adopted UNSC Resolution 1929 emphasizes, “the potential connection between Iran’s revenues derived from its energy sector and the funding of Iran’s proliferation-sensitive nuclear activities.”⁶ The resolution also expresses concern that “chemical process equipment and materials required for the petrochemical industry have much in common with those required for certain sensitive nuclear fuel cycle activities.”⁷

At a summit on June 17, 2010, E.U. officials stated that sanctions had “become inevitable,” and announced that the E.U. would ban new investment, technical assistance and technology transfers in connection with Iran’s natural gas and oil industry.⁸ On July 26, 2010, the E.U. approved these sanctions on Iran’s energy sector.⁹ On the same day, the Canadian government adopted similar measures banning new investment in Iran’s oil and natural gas sectors.¹⁰

Despite these developments, a sober assessment of energy sanctions shows that they have significant room for improvement. To counter the threat of international sanctions, Iran

⁴ “UPDATE 1-Iran Needs \$25 bln/year in Energy Investment-Report,” *Reuters*, May 10, 2010.

(<http://in.reuters.com/article/id/INLDE6490X420100510>)

⁵ Kenneth Katzman, “The Iran Sanctions Act (ISA),” *Congressional Research Service*, June 4, 2009, p. 4.

(<http://italy.usembassy.gov/pdf/other/rs20871.pdf>)

⁶ UN Security Council, 6335th Meeting, “Resolution 1929 (2010),” June 9, 2010, p. 3.

(http://www.defenddemocracy.org/images/UNSC_Resolution_1929_6_9_10.pdf)

⁷ UN Security Council, 6335th Meeting, “Resolution 1929 (2010),” June 9, 2010, p. 3.

(http://www.defenddemocracy.org/images/UNSC_Resolution_1929_6_9_10.pdf)

⁸ Paul Harrington, “EU Hits Iran with Tougher Sanctions Over Nuclear Row,” *AFP*, June 17, 2010.

(<http://www.google.com/hostednews/afp/article/ALeqM5gKj7RH7a119u02uMKMH9e3Dk3YVQ>)

⁹ James G. Neuger and Jonathan Stearns, “EU to Impose Sanctions on Iran in Bid to Halt Nuclear Drive,” *Bloomberg*, July 26, 2010. (<http://www.bloomberg.com/news/2010-07-26/eu-will-impose-sanctions-on-iran-to-ban-oil-investment-scrutinize-banks.html>)

¹⁰ Campbell Clark, “Canada to Impose Tough New Sanctions on Iran,” *The Globe & Mail*, July 25, 2010.

(<http://www.theglobeandmail.com/news/politics/canada-to-impose-tough-new-sanctions-on-iran/article1651467/>)

has signed major energy deals with countries not likely to cooperate with sanctions, including China, Russia, Turkey, and Venezuela. Iran plans substantial upgrades to seven of its nine existing oil refinery facilities. Iran also has decades of experience adopting countermeasures to circumvent sanctions. It is highly adept at using cutouts, smuggling, and front companies to procure the goods, technology, equipment, and services that are vital to its energy sector. Much of this activity takes place through Dubai, as well as other points of transshipment, including Malaysia, Hong Kong and Turkey.

Furthermore, companies without significant exposure to U.S. energy markets may calculate that the rewards of doing business with Iran outweigh the risks. Other companies will note Washington's relatively weak historical record of enforcing energy sanctions and determine that their interests are not in real jeopardy. Asian and Persian Gulf countries will watch carefully the level of American and European commitment to enforcement with the understanding that they will never be expected to do more than Washington and Brussels.

Nevertheless, sanctions still cause trouble for the Iranian regime. The mere possibility of meaningful energy sanctions has already achieved tangible results: ten of Iran's top suppliers have reportedly stopped selling gasoline to Iran after calculating that the political risks of continued trade were too high. They include: BP, Vitol, Trafigura, Glencore, Total, Shell, Reliance, Lukoil, Petronas and the Independent Petroleum Group.¹¹

Most Western banks have also stopped underwriting gasoline shipments to Iran. Four major insurance companies — Lloyd's of London, Munich Re, Hannover Re and Allianz — announced they would stop or sharply reduce their underwriting for Iran's gasoline trade.¹² Numerous energy companies are terminating or significantly reducing their investments in Iranian oil and natural gas. Foreign companies that were already cutting back their energy ties to Iran before the legislation passed now have even more incentive to do so.¹³

The focus on energy sanctions has also reshaped the debate in Washington. It is no longer a discussion over how to achieve a "grand bargain" with the Iranian regime. Rather, the

¹¹ "Petronas Halts Petrol Sale to Iran," *Emirates Financial News*, April 15, 2010. (<http://www.emiratesfn.com/news/newsfull.php?newid=356995>); and Stanley Carvalho, "Western Oil Firms Stop Business with Iran," *Reuters*, June 28, 2010. (<http://uk.reuters.com/article/idUKDAH85080620100628>); and "Companies Cutting Ties Their Iran Energy Ties, *IranEnergyProject.org*, accessed July 26, 2010. (<http://www.iranenergyproject.org/hotsheet/>)

¹² Katherine Blackler, "Allianz Will Not Renew Business in Iran," *Reinsurance*, February 19, 2010. (<http://www.postonline.co.uk/reinsurance/news/1592838/allianz-renew-business-iran>); and Jamie Dunkley, "Lloyd's of London Backs US Sanctions on Iran," *The Telegraph*, July 9, 2010. (<http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/insurance/7882144/Lloyds-of-London-backs-US-sanctions-on-Iran.html>)

¹³ "Factbox—Foreign companies step away from Iran," *Reuters*, July 23, 2010. (<http://af.reuters.com/article/energyOilNews/idAFLDE66M16X20100723>); and "Factbox – Sanctions and fuel supplies to Iran," July 23, 2010. (<http://af.reuters.com/article/energyOilNews/idAFLDE66L1VR20100723?sp=true>)

debate now focuses on how to deter an aggressive regime that is dedicated to pursuing nuclear weapons, supporting terrorism, and repressing its own people.

The Iranian regime claims it can withstand energy sanctions. But the efficacy of its countermeasures, including expanding refinery capacity and introducing flex-fuel cars, is greatly exaggerated. Its most effective option, a sharp reduction in gasoline subsidies, could force Iran's already skyrocketing inflation rates to double or triple.

Iran's energy sector is now under more pressure than it has been in recent memory, and that this happened without a concerted effort by the White House to actually enforce sanctions legislation. While U.S. efforts to ban foreign energy investment in Iran began with the passage of the *Iran and Libya Sanctions Act of 1996* (amended in 2006 to the *Iran Sanctions Act*), authorizing the President to sanction foreign firms investing \$20 million or more in Iran's energy sector in any single year, no president has ever sanctioned even one. Historically, sanctions have been deterred by a fear of a backlash from the major players in Iran's energy business, some of which have significant trade relations with the United States.

Imagine what would happen if the President used his new sanctions authority.

Meanwhile, as the U.S., the E.U. and U.N. enact sanctions, a growing number of Iranians no longer believe their leaders' attempts to blame Washington for Iran's diplomatic isolation and its stagnating economy. In November 2008, a group of 60 Iranian economists criticized President Mahmoud Ahmadinejad for his "tension-creating" foreign policy that "scared off foreign investment and inflicted heavy damage on the economy."¹⁴ They noted that sanctions had cost Iran billions of dollars by forcing it to rely on middlemen for imports and exports. Indeed, many Iranians despise the regime not only for its human rights abuses but also because of the disastrous state of the economy, which suffers from double-digit inflation and soaring unemployment.¹⁵

For energy sanctions to be a game changer, however, they have to be crushing. Supreme Leader Ayatollah Ali Khamenei's commitment to developing nuclear weapons is probably as strong as was Ayatollah Ruhollah Khomeini's determination to destroy Saddam Hussein in the Iran-Iraq War. The shock that stopped Khomeini — U.S. naval operations that threatened Iran's energy exports and imports and thus his regime's survival — is instructive. Sanctions must complement the only thing that has so far rattled the regime: the pro-democracy Green Movement.

These developments present opportunities for Congress and President Obama to place unprecedented pressure on the Iranian regime and persuade Iran's leaders that nuclear

¹⁴ Borzou Daragahi, "Economists in Iran Criticize Ahmadinejad," *Los Angeles Times*, November 10, 2008. (<http://articles.latimes.com/2008/nov/10/world/fg-iran10>)

¹⁵ Babak Dehghanpisheh, "In Iran, Inflation Could Threaten Regime," *Newsweek*, February 5, 2010. (<http://www.newsweek.com/blogs/wealth-of-nations/2010/02/05/in-iran-inflation-could-threaten-regime.html>)

weapons are not a guarantee of regime survival but rather a possible catalyst of its demise.

Sanctions and the Iranian People

Iranians are hungry for political change, but such a transformation will not necessarily be immediate. It took nine years for Lech Walesa's Solidarity strike at Gdansk to culminate in the collapse of communist rule in Poland. And while U.S. policymakers still hold out hope for a free Iran in the long-term, it is prudent to prepare for a more dangerous Iranian regime in the short-term.

Conventional wisdom holds that imposing harsher energy sanctions on the Iranian regime will have little effect on Ayatollah Khamenei, President Ahmadinejad and the Islamic Revolutionary Guard Corps, the entity largely responsible for Iran's nuclear program and for the brutal crackdown on Iran's pro-democracy Green movement.

Prominent Green leaders like Mir Hossein Mousavi criticize international sanctions on Iran but blame the regime for Iran's increasing isolation.¹⁶ Mousavi, for his part, has called for a referendum on Iran's nuclear program, perhaps recognizing that a nuclear weapons program is not as popular as the regime has claimed.¹⁷ However, other Iranian dissidents go farther and welcome robust penalties against Iran's energy business. Mohsen Makhmalbaf, a distinguished film director who serves as a sort of spokesman for the Green movement, neatly captured the need to increase global economic pressure on the Iranian elites. "The Revolutionary Guards are terrorists. They are in Iraq, Afghanistan and Lebanon. They tortured people in Iran. They rape people in prisons. If you explain to the Iranian people that you are sanctioning their enemies, they will support you," he told the *Guardian*.¹⁸

An internal debate over the need for sanctions is not without precedent. In the 1980s, for example, Archbishop Desmond Tutu and other activists initially opposed sanctions against the apartheid regime for fear that they would harm black South Africans.¹⁹ They later reversed their position when they saw that sanctions would marginalize and undermine the government that was oppressing them.

¹⁶ Ladane Nasser, Henry Meyer and Ali Sheikholeslami, "Iran Opposition Struggles as Ahmadinejad Gets Boost," *Bloomberg*, June 9, 2010. (<http://www.bloomberg.com/news/2010-06-08/iran-opposition-struggles-as-nuclear-sanctions-wrangle-boosts-ahmadinejad.html>); and

"Iranian Opposition Leader Blames Sanctions on Ahmadinejad," *The Media Line*, July 8, 2010. (<http://newsblaze.com/story/20100708112334zzzz.nb/topstory.html>)

¹⁷ Bahram Rafiee, "Mousavi: The Nation is Not Told How Dangerous the Situation Is," *Rooz Online*, July 13, 2010. (<http://www.roozonline.com/english/news/newsitem/article/2010/july/13//mousavi-the-nation-is-not-told-how-dangerous-the-situation-is.html>)

¹⁸ Ian Black, "Iran Should Face Smarter Sanctions, Says Mohsen Makhmalbaf," *The Guardian*, November 25, 2009. (<http://www.iranenergyproject.org/277/iran-should-face-smarter-sanctions-says-mohsen>)

¹⁹ "Desmond Tutu," *Encyclopedia of World Biography*, accessed July 13, 2010. (<http://www.notablebiographies.com/Tu-We/Tutu-Desmond.html>)

The Iranian regime may be near its tipping point. The harder it cracks down on democratic activists, the less support it enjoys, even among conservative elites. The economic strikes in summer 2010 by the influential Bazaaris, the Iranian merchant class that played an important role in the downfall of the Shah of Iran in 1979, suggest that discontent for the regime could spread beyond the democracy movement.

Sanctions can accelerate Iran's economic crisis. For example, riots followed Tehran's decision in 2007 to ration gasoline supplies. Drivers torched gas stations. A concerned Iranian parliament quickly pressed the government to scrap the rationing plan.²⁰

Last year, the Iranian government announced plans to reduce subsidies for energy and basic commodities.²¹ The decision was motivated by the regime's desire to reduce soaring demand for cheap gasoline (as a way to counter the effects of gasoline sanctions) and to save the Iranian treasury billions of dollars in subsidy support payments. However, if the government allows the prices of gasoline and other commodities to rise to market levels, it could drive Iran's current inflation rate from unofficial estimates of 20-25 percent²² to as high as 40 percent²³ — compounding the country's economic problems and fanning the flames of domestic discontent.

The level of discontent is high in Iran. Sanctions could accelerate the political transformation that many Iranians seek. This could increase the likelihood of stopping the Iranian nuclear weapons program.

What Can the U.S. Do?

Recommendations on Enforcement

1. Penalize companies that continue to violate U.S. sanctions laws.

The Obama administration should impose stiff but selective penalties against companies that continue to invest in the Iranian energy sector and violate U.S. sanctions law. Many companies will be watching closely the administration's commitment to sanctions enforcement and searching for signs that the U.S. is not serious. European allies will not take their own steps to enforce their own sanctions until they can be persuaded that their companies will not lose business to Chinese, Russian, Turkish, and other competitors. For these reasons, the Obama Administration must penalize companies from countries that continue to violate U.S. sanctions laws.

²⁰ "Iran Fuel Rations Spark Violence," *BBC News*, June 27, 2007.
(http://news.bbc.co.uk/2/hi/middle_east/6243644.stm)

²¹ Henry Meyer, "Iran Government Subsidy Cuts to Reduce Fuel Imports, Central Banker Says," *Bloomberg*, May 16, 2010. (<http://www.bloomberg.com/news/2010-05-16/iran-government-subsidy-cuts-to-curb-sanction-impact-central-banker-says.html>)

²² Hossein Askari, "Iran on the Edge," *Foreign Policy*, November 3, 2009.
(http://www.foreignpolicy.com/articles/2009/11/03/iran_on_the_edge?page=0,0)

²³ Hossein Askari, "Iran on the Edge," *Foreign Policy*, November 3, 2009.
(http://www.foreignpolicy.com/articles/2009/11/03/iran_on_the_edge?page=0,0)

The following companies are high priority candidates for sanctions:

1. Aker Solutions (Norway) – Aker Solutions and its subsidiaries continue to operate in Iran. The firm's subsidiary, Aker Wirth has been active in a construction project that is overseen by Sahel Consulting Engineers, a company owned by the IRGC.²⁴
2. China National Petroleum Company (CNPC) (China) – CNPC is active in several of Iran's oil and gas fields, including the North and South Azadegans oil fields and Iran's massive South Pars gas field.²⁵
3. Daelim Industrial Corporation (South Korea) – The South Korean firm is active in a number of projects in Iran including a \$600 million project to develop a phase of South Pars gas field.²⁶
4. Elektrizitäts-Gesellschaft Laufenburg (EGL) (Switzerland) – The National Iranian Gas Export Company signed a deal to supply EGL with gas for up to 25 years in February 2008.²⁷
5. Gazprom (Russia) – Russian energy giant Gazprom has been involved in both upstream and downstream activities in Iran, including the Azar oilfield development project and the Iran-Armenia gas pipeline.²⁸
6. Haldor Topsoe (Denmark) – The Danish firm has been active in a number of petrochemical projects in Iran. Currently, the company is licensing technology and providing support services to several Iranian firms for two methanol plants in Iran.²⁹

²⁴ Emanuele Ottolenghi, "The Iranian Shell Game," *Commentary*, July – August 2008, p. 52. (http://www.commentarymagazine.com/viewpdf.cfm?article_id=11460)

²⁵ Alison Klayman, "China Works to Raise Mideast Profile," *Voice of America*, January 15, 2009. (<http://www1.voanews.com/english/news/a-13-2009-01-15-voa14-68810252.html?CFTOKEN=60235739&jsessionid=003013ee5b02ab62087b7f65367a40c754f2&CFID=285053156>); and "CNPC replaces Total at South Pars II," *Upstream Online*, June 3, 2009. (<http://www.upstreamonline.com/live/article179964.ece>); and "Iran, China Sign Major Deal to Develop South Azadegan," *Rig Zone*, September 30, 2009. (http://www.egyptoil-gas.com/read_article_international.php?NID=1139)

²⁶ "Profiting From Iran, and the U.S.," *The New York Times*, March 12, 2010. (<http://www.nytimes.com/interactive/2010/03/06/world/iran-sanctions.html>)

²⁷ Carl Mortished, "Swiss Brush Aside Criticism Over Gas Contract with Iran," *The Times*, March 24, 2008. (http://business.timesonline.co.uk/tol/business/industry_sectors/utilities/article3607258.ece)

²⁸ Aresu Egbali, "Gazprom Signs Deal to Develop 2.2 Billion Barrel Azar Oil Field in Iran," *Platts Oilgram News*, November 3, 2009. (<http://www.iranenergyproject.org/508/gazprom-signs-deal-to-develop-22-billion-barrel>); and "Gazprom to Invest USD 200 Million in Iran Armenia Gas Pipeline," *Steel Guru*, June 8, 2008. (http://www.steelguru.com/middle_east_news/Gazprom_to_invest_USD_200_million_in_Iran_Armenia_gas_pipeline/49499.html)

²⁹ "Topsoe Signs Contract for Two Large Methanol Plants with Marjan Petrochemical and Kimiaye Pars," *Haldor Topsoe, Press Release*, March 13, 2009. (<http://www.topsoe.com/News/News/2009/130309.aspx>)

7. Inpex (Japan) – Inpex has remained an investor in the development of Iran’s Azadegan oilfield.³⁰
8. The Linde Group (Germany) – Linde has provided design and technology for a number of petrochemical projects in Iran, including those linked to South Pars and the Iran LNG Project.³¹
9. LyondellBasell (Netherlands) – Dutch firm, LyondellBasell has supplied petrochemical technology to Iran for a number of its polyethylene plants.³²
10. Oil & Natural Gas Corporation (ONGC) (India) – India’s ONGC is active in more than one project in Iran including the Farsi block and South Pars.³³
11. Petróleos de Venezuela, S.A. (PDVSA) (Venezuela) – Iran and Venezuela have signed numerous deals to jointly develop their energy resources, including forming a joint oil company to manage their operations in other countries.³⁴
12. Sinopec (China) – The Chinese-firm has signed numerous deals with Iran in both upstream and downstream activities.³⁵
13. SKS Ventures (Malaysia) – SKS Ventures has made several deals with Iran, including gas field development in Iran and the construction of refineries in Malaysia.³⁶

³⁰ “FACTBOX: Iran’s Major Oil Customers, Energy Partners,” *Reuters*, August 18, 2009. (<http://www.reuters.com/article/idUSTRE57H1UJ20090818>)

³¹ “Linde erhält Auftrag für Erdgasanlage im Iran,” *Handelsblatt* (Germany), September 6, 2000. (<http://www.handelsblatt.com/archiv/linde-erhaelt-auftrag-fuer-erdgasanlage-im-iran:325195>); and Amanda Battersby, “Iran LNG under Starter’s Orders,” *Upstream Online*, March 11, 2008. (<http://www.upstreamonline.com/live/article150376.ece>)

³² Joseph A. Christoff, “Firms Reported in Open Sources as Having Commercial Activity in Iran’s Oil, Gas, and Petrochemical Sectors,” U.S. Government Accountability Office, March 23, 2010, p. 15. (<http://www.gao.gov/new.items/d10515r.pdf>)

³³ “US Names ONGC, IOC for Doing Biz with Iran,” *PTI*, May 14, 2010. (<http://economictimes.indiatimes.com/news/news-by-industry/energy/oil--gas/US-names-ONGC-IOC-for-doing-biz-with-Iran/articleshow/5930807.cms>)

³⁴ “Energy Cooperation Drives a Murky Venezuela-Iran Relationship,” *OilPrice.com*, June 6, 2010. (<http://oilprice.com/Geo-Politics/International/Energy-Cooperation-Drives-a-Murky-Venezuela-Iran-Relationship.html>)

³⁵ “Firms Reported in Open Sources as Having Commercial Activity in Iran’s Oil, Gas, and Petrochemical Sectors,” U.S. Government Accountability Office, March 23, 2010, p. 17. (<http://www.gao.gov/new.items/d10515r.pdf>)

³⁶ “Malaysia to Invest \$20bn in Iran’s Fields,” *PressTV* (Iran), December 8, 2009. (<http://www.presstv.ir/detail.aspx?id=113169§ionid=351020103>); and “Iran and Malaysia Sign \$14 Billion of Oil and Gas Cooperation Agreements,” *Industrial Info Resources*, December 15, 2008. (<http://www.pump-zone.com/global-news/global-news/iran-and-malaysia-sign-14-billion-of-oil-and-gas-cooperation-agreements.html>)

14. ThyssenKrupp (Germany) – ThyssenKrupp has been active in Iran since the 1970s and Iran's Foreign Investment Company is a shareholder in the Germany company.³⁷
15. WorleyParsons (Australia) – The Australian engineering firm has provided design and engineering for a number of projects in Iran including gas processing facilities, and drilling platforms.³⁸

2. *Enforce sanctions that prevent companies – mainly European -- from supplying key technologies, equipment, and know-how to Iran's energy sector.*

Iran depends on foreign technology, goods, and services to develop its energy resources. While Chinese and Russian companies can provide significant capital for both natural gas and oil projects, Iran too often depends on western subcontractors for the technology, equipment, and know-how it needs to exploit its natural gas resources. Much of that comes from one European nation: Germany.³⁹

The Obama administration should encourage European leaders to enforce the sanctions announced by the EU this week by prohibiting companies in its jurisdiction from providing investment, technology, and technical assistance to Iran under current and future contracts. This should have an immediate impact on German-Iranian ties.

More broadly, the rest of the world will be watching how the E.U. implements its own sanctions. The E.U. is Iran's largest trading partner, so whatever it does will become a "ceiling" particularly for Gulf and Asian countries that are unlikely to do more.

3. *Enforce sanctions against joint ventures, partnerships, and investments in foreign energy projects involving Iranian entities.*

Iran has pursued partnerships with foreign energy companies to frustrate American attempts to build international consensus for sanctions enforcement. These include: natural gas projects off the coast of Scotland, Croatia, and Azerbaijan; investments in European energy and infrastructure companies; and refineries in Indonesia, Malaysia, and Sri Lanka. This grants Tehran access to technology and expertise to develop its own energy resources, influence over foreign partners, and additional revenues.⁴⁰

³⁷ "German Business with Iran: The Example ThyssenKrupp," *Stop the Bomb*, accessed July 26, 2010. (<http://de.stopthebomb.net/en/start/germany/d-iran/thyssenkrupp.html>)

³⁸ "New Player Set to Review Iran's South Pars 11 FEED," *Upstream*, May 9, 2010. (<http://www.bedigest.com/NEWS/39013.aspx>); and "Iran Awards South Pars Design Deal to Worley Parsons," *Middle East Economic Digest*, April 22, 2008. (<http://www.gasandoil.com/goc/company/cnm82025.htm>)

³⁹ "Iran's Energy Technology Partners," *IranEnergyProject.org*, accessed July 26, 2010. (<http://www.iranenergyproject.org/natural-gas/>)

⁴⁰ Massimo Calabresi, "Sleeping with the Enemy: BP's Deals with Iran," *Time*, June 16, 2010. (<http://www.time.com/time/nation/article/0,8599,1996921,00.html>); *The Middle East and North Africa 2004* (Routledge, 2004) p.402. (Available on Google Books); "Iran to Invest \$1.7b in Azeri Gas Field,"

The *Comprehensive Act* partially addressed a loophole in U.S. sanctions laws that overlooked these business relationships. The Obama administration must now report to Congress every six months with a list of companies involved in overseas projects with the Iranian regime. Unless it waives these sanctions, the administration must apply tough penalties to companies involved in joint ventures, partnerships, or investments with Iranian entities.

The U.S. should encourage the E.U. and other allies to further restrict these activities. While E.U. will bar its own companies from entering into joint ventures, investments, and other partnerships with Iran's energy sector, it should extend its ban to overseas Iranian energy projects, where Iran-controlled entities are currently partnering with European companies in Europe. These projects give the Iranian regime access to key technology, technical expertise and influence over European energy sources and their European energy partners.

4. Designate additional Iranian Revolutionary Guard Corps entities in Iran's energy business.

The role of the IRGC in Iran's energy industry represents both a challenge and an opportunity to policymakers seeking to use energy sanctions to influence regime behavior. On one hand, the Iranian energy industry suffers from an acute shortage of capital and expertise exacerbated by the fact that the IRGC continues to replace competent energy technocrats with its inexperienced loyalists. On the other hand, energy sanctions provide an opportunity to target IRGC persons and companies — which are deeply unpopular with the Iranian people — and convince foreign companies to stop doing business with IRGC entities.

The U.S. Treasury Department should add to its 2007 and 2010 designations of the IRGC by designating other entities that are dominant players in the Iranian energy industry. Treasury has taken significant steps in this direction by designating Khatam al-Anbiya

Press TV (Iran), January 10, 2009. (<http://payvand.com/news/09/jan/1099.html>); "Azerbaijan - Socar & The PSAs," *APS Review Gas Market Trends*, July 3 2006. (<http://www.allbusiness.com/sector-21-mining/oil-gas-extraction-crude/1183283-1.html>); "Iran and Spain to Build LNG Terminal in Croatia," *Croatian Times*, June 9, 2010. (<http://www.iranoilgas.com/news/details2/?type=news&p=current&newsID=5931&restrict=no>); Benjamin Weinthal, "Nazi-Era Corporate Behavior Repeated," *The Jerusalem Post*, January 22, 2010. <http://www.jpost.com/Home/Article.aspx?id=166381>; "FACTBOX: Iran's Major Oil Customers, Energy Partners," *Reuters*, August 18, 2009. (<http://www.reuters.com/article/idUSTRE57H1UJ20090818>); "FACTBOX-Indonesia plans to upgrade ageing oil refineries," *Intellasia/Reuters*, January 2, 2010. (<http://www.intellasia.net/news/articles/resources/111267566.shtml>); "New Malaysian Refinery Invites Iran to Take Stake," *Press TV*, March 23, 2007. (<http://www.gasandoil.com/goc/company/cnm71533.htm>); "Iran, Malaysia to Push ahead with US\$7 Billion Joint Venture," *Business and Economy Digest*, August 16, 2009 (<http://www.bedigest.com/NEWS/27237.aspx>); and Ranga Sirilal, "Iranian President Launches Sri Lanka Refinery Upgrade," *Reuters*, April 29, 2008. (<http://in.reuters.com/article/idINIndia-33302020080429>)

(Ghorb) and four of its (reported 812) affiliates.⁴¹ It also added 22 insurance, petroleum, and petrochemicals companies to the Iranian Transactions Regulations (ITR) list, a slate of entities inside and outside Iran with which American firms cannot do business.

It is worth noting here that no one should be fooled by recent reports that Ghorb is pulling out of South Pars, Iran's large natural-gas field.⁴² Ghorb will remain a major player in Iran's energy industry through myriad front companies and affiliates.

When it has evidence that Iranian entities support proliferation or terrorism activities, Treasury should go beyond the ITR list and designate these entities on proliferation and terrorism grounds. It should designate Kala Naft, the overseas procurement arm of the National Iranian Oil Company, which is on British and Japanese watch lists for its connection to proliferation activities;⁴³ the Swiss-based NaftIran, a key player in overseas energy projects, and a “major strategic asset” for Iran;⁴⁴ and the Pars Oil & Gas Company, a major player in the Iranian natural gas industry with ties to the IRGC, according to Iranian sources.⁴⁵

The Obama administration should encourage the E.U., Canada, Australia, and other allies to add these IRGC entities to their own sanctions packages. Companies will be less likely to assume the significant legal and reputational risk of doing business in the Iranian energy sector if the U.S. and its allies take these actions.

The banking sector provides a useful model for enforcement: The foreign financial institutions that terminated or reduced their business with Iran were not legally bound to comply with U.S. sanctions. However, after Treasury revealed Iran's extensive use of deceptive financial practices and front companies, foreign bankers complied on their own. These institutions calculated that the costs of doing business in Iran — and being publicly linked to bad actors there — outweighed the benefits, and presented a real risk of losing access to U.S. financial markets.

Fines have also been instrumental to enforcement. Financial institutions took note when, in 2005, the U.S. government fined Dutch bank ABN Amro \$80 million for inadequate compliance with U.S. sanctions on Iran and Libya under the *Bank Secrecy Act*.⁴⁶ They

⁴¹ Massimo Calabresi, “Sleeping with the Enemy: BP's Deals with Iran,” *Time*, June 16, 2010. (<http://www.time.com/time/nation/article/0,8599,1996921.00.html>)

⁴² Benoit Faucon and Farnaz Fassihi, “Sanctions Force a Retreat in Iran,” *Wall Street Journal*, July 17, 2010. (http://online.wsj.com/article/NA_WSJ_PUB:SB10001424052748704913304575371150400414946.html)

⁴³ Kala Naft, Iran Watch (<http://www.iranwatch.org/suspect/records/Kala-Naft.html>)

⁴⁴ Massimo Calabresi, “Sleeping with the Enemy: BP's Deals with Iran,” *Time*, June 16, 2010. (<http://www.time.com/time/nation/article/0,8599,1996921.00.html>)

⁴⁵ Mark Dubowitz, Confidential Report submitted to the U.S. Treasury Department, Foundation for Defense of Democracies, 2010.

⁴⁶ Barnaby J. Feder, “ABN to Pay \$80 Million for Violations,” *The New York Times*, December 20, 2005. (<http://www.nytimes.com/2005/12/20/business/worldbusiness/20bank.html>)

also took note in 2009, when the U.S. imposed \$350 million in fines on Britain's Lloyds Bank⁴⁷ and \$536 million on Credit Suisse for violations of Iran sanctions laws.⁴⁸

The U.S. can use the same approach to dissuade Iran's energy partners from investing in the Iranian energy sector or exporting refined petroleum products, or energy-related technology, goods and services to the Iranian regime.

5. Cut Iran's energy partners from all U.S. government contracts.

On May 12, 2010, the Senate Committee on Homeland Security and Governmental Affairs held a hearing in an attempt to understand why the U.S. government continues to award contracts to companies that do business with Iran. The hearing followed a March 2010 report published in the *New York Times* noting that the U.S. had awarded "more than \$107 billion in contract payments, grants and other benefits" over ten years to 74 foreign and multinational companies doing business in Iran.⁴⁹

Section 102 of the *Comprehensive Act* requires all U.S. government contractors to certify that neither they, nor any person under their control, engage in any activity subject to Iran sanctions. False certifications shall result in the termination of applicable contracts, and suspension or debarment of the prospective contractor for up to three years.

The Obama administration should enforce this provision by banning any firm subject to Iran sanctions from government contracts, particularly those providing fuel supplies to the U.S. Department of Defense, the largest government purchaser of petroleum products.⁵⁰

6. Impose stiff penalties on companies that sell refined petroleum to Iran.

In recent years, six companies have served as Iran's primary gasoline providers: the Swiss-Dutch energy trading giants Vitol and Trafigura, the Indian multinational Reliance Industries, the Swiss trader Glencore, the Dutch-British energy firm Shell, and the French energy firm Total. All of these companies — many with long-standing ties to Iran — have reportedly terminated or announced their intent to terminate gasoline sales to Iran. In addition, most Western banks have ceased underwriting gasoline shipments to Iran. Four insurance companies — Lloyd's of London, Munich Re, Allianz, and Hannover Re — have reportedly exited the market or sharply reduced their Iranian business ties.

⁴⁷ Karen Freifeld, "Lloyds TSB to Pay \$350 Million to Settle Probe (Update1)," *Bloomberg*, January 10, 2009. (<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aeBCUImC3IMk&refer=us>)

⁴⁸ Joshua Gallu, Karen Freifeld and Cary O'Reilly, "Credit Suisse to Pay \$536 Million in U.S. Settlement (Update3)," *Bloomberg*, December 16, 2009.

(<http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aG1wylpbsqCU>)

⁴⁹ Jo Becker and Ron Nixon, "U.S. Enriches Companies Defying Its Policy on Iran," *The New York Times*, March 6, 2010. (<http://www.nytimes.com/2010/03/07/world/middleeast/07sanctions.html>)

⁵⁰ Spencer Swartz and Steve Stecklow, "U.S. Bill Takes Aim at Iran's Oil Partners," *Wall Street Journal*, May 25, 2010. (<http://online.wsj.com/article/SB10001424052748704792104575264561801614780.html>) The Pentagon is the world's single-largest oil consumer, burning around 400,000 barrels a day.

Others firms, however, stepped in to replace them. They included the Kuwait-based Independent Petroleum Group, Russia's LUKOIL and Malaysia's Petronas. And while these companies have reportedly stopped their supplies, they may decide at any time to re-enter the market unless the Obama administration demonstrates that it is serious about enforcing sanctions against those continuing to supply Iran.

Today, Iran's gasoline supplies are provided by:

- *Chinaoil*, the trading arm of China National Petroleum Company (CNPC), has taken advantage other sellers leaving the Iranian market.⁵¹ According to Reuters, the company "sold two gasoline cargoes for April delivery to Iran." These 2010 deliveries were the first Chinaoil direct sales to Iran since January 2009.⁵² Reports indicate that Chinaoil remains one of Iran's remaining gasoline suppliers.
- *Unipet*, the trading arm of China's Sinopec, booked a vessel in April 2010, "to load 250,000 barrels in Singapore, with options to discharge in the Gulf. The cargo was likely to go to Iran, trade sources said."⁵³ Unipet previously sold gasoline to Iran between 2001 and 2004.⁵⁴ While Sinopec did not deliver gasoline to Iran in May of this year, it reportedly delivered 600,000 barrels in June.⁵⁵ Industry sources also report that Unipet had begun purchasing gasoline from independent traders in the United Arab Emirates and reselling the fuel to Iran.⁵⁶
- China's *Zhuhai Zhenrong* has been shipping a cargo or two each month to Iran for at least a year, according to Reuters.⁵⁷ While the Chinese company has not publicly announced that it is ceasing gasoline deliveries to Iran, recent press reports no longer indicate that it is a supplier.
- Turkish oil refiner *Tupras* first supplied Iran with gasoline in June 2010 after an eighteen-month pause in deliveries.⁵⁸ July reports indicate that Turkey is expected to deliver four to five gasoline cargoes to Iran.⁵⁹

⁵¹ Simon Webb, "UPDATE 2-Iran Relies on Friendly Powers for Fuel Supplies," *Reuters*, July 8, 2010. (<http://uk.reuters.com/article/idUKLDE6671UA20100708>)

⁵² Luke Pachymuthu and Seng Li Peng, "Exclusive: China's Top Oil Firms Sell Gasoline to Iran-Trade," *Reuters*, April 14, 2010. (<http://www.iranenergyproject.org/373/exclusive-chinas-top-oil-firms-sell-gasoline-to>)

⁵³ Luke Pachymuthu and Seng Li Peng, "Exclusive: China's Top Oil Firms Sell Gasoline to Iran-Trade," *Reuters*, April 14, 2010. (<http://www.iranenergyproject.org/373/exclusive-chinas-top-oil-firms-sell-gasoline-to>)

⁵⁴ "Sinopec Ships 600,000 Barrels of Gasoline to Iran," *Reuters*, May 25, 2010. (<http://english.alroya.com/content/sinopec-ships-600000-barrels-gasoline-iran>)

⁵⁵ "Sinopec Ships 600,000 Barrels of Gasoline to Iran," *Reuters*, May 25, 2010. (<http://english.alroya.com/content/sinopec-ships-600000-barrels-gasoline-iran>)

⁵⁶ Luke Pachymuthu and Chen Aizhu, "China's Sinopec Ships Gasoline from UAE to Iran," *Reuters*, June 1, 2010. (<http://www.lhymarkets.com/html/news/2010/6/1/1275387396nLDE64T029.html>)

⁵⁷ "China Firms Selling Fuel to Iran as U.S. Sanctions Loom," *Reuters*, September 23, 2009. (<http://www.reuters.com/article/idUSTRE58M1BK20090923>)

⁵⁸ Simon Webb, "UPDATE 2-Iran Relies on Friendly Powers for Fuel Supplies," *Reuters*, July 8, 2010. (<http://uk.reuters.com/article/idUKLDE6671UA20100708>)

In the month of July, Tupras and Unipac reportedly provided Iran with three cargoes, with a fourth on its way from Venezuela. This is significantly less than the 11-13 cargoes Iran requires during the summer months, suggesting that the threat of sanctions is having an impact.⁶⁰ Gasoline is reportedly also reaching Iran by way of smuggling operations from Iraqi Kurdistan.⁶¹

In addition to smuggling, it is likely that other suppliers without significant exposure to U.S. markets will emerge. Companies that have terminated their business ties to Iran may also decide to re-enter the gasoline supply market and work through third and fourth parties to hide their role. Indeed, a number of companies that previously sold gasoline to Iran have a long history of sanctions-busting and deep experience in working through front companies and cutouts.

To discourage this behavior, the Obama administration will need to track the gasoline trade carefully and impose heavy penalties on select gasoline suppliers. These penalties will send a message to the trade that violators of U.S. sanctions are taking significant financial and reputational risks by trading with Iran.

7. Establish a bipartisan Congressional Iran Sanctions Enforcement Commission.

The Iranian energy industry is complicated, fluid and opaque. It involves thousands of Iranian and foreign entities with operations inside and outside Iran. The Iranian regime also makes extensive use of front companies to hide their activities. To enforce sanctions effectively, Congress must have access to open source and classified material, as well as mechanisms to ensure regular review and dissemination of relevant information. Numerous government agencies collect information on Iran's energy business, including the Energy Information Administration, the Government Accountability Office, the U.S. Treasury Department's Office of Intelligence and Analysis and Office of Foreign Assets Control, and the relevant U.S. intelligence agencies, among others.

To effectively monitor and investigate the Iranian energy sector at a sufficient level of granularity, Congress should establish a Bipartisan Commission on Iran Sanctions Enforcement dedicated to the enforcement of U.S. sanctions against Iran. The Commission would conduct comprehensive research on Iran's energy sector, using open-source and classified information from government and third-party sources. It should conduct regular assessments of the sanctions regime, hold congressional hearings, and make recommendations to Congress to ensure tougher sanctions enforcement.

⁵⁹ Simon Webb, "UPDATE 2-Iran Relies on Friendly Powers for Fuel Supplies," *Reuters*, July 8, 2010. (<http://uk.reuters.com/article/idUKLDE6671UA20100708>)

⁶⁰ Amana Bakr and Luke Pachymuthu, "Iran Fuel Imports Nosedive as Sanctions Bite—Source," *Reuters*, July 26, 2010. (<http://af.reuters.com/article/energyOilNews/idAFLDE66P0RF20100726?sp=true>)

⁶¹ Sam Dagher, "Smugglers in Iraq Blunt Sanctions Against Iran," *New York Times*, July 8, 2010. (<http://www.nytimes.com/2010/07/09/world/middleeast/09kurds.html>)

8. *Adopt a U.S./E.U. sanctions enforcement model similar to that used successfully in implementing sanctions against Serbia.*

The Obama administration should consider adopting U.S./E.U. sanctions enforcement model like the one used against Serbia during the war in Yugoslavia. To ensure accountability of states and companies, the U.S. and E.U. created a cooperative venture in the mid-1990s called the Sanctions Assistance Mission, which interfaced with the UN sanctions committee and various intergovernmental organizations, law enforcement, and customs agencies, holding companies to account.

These sanctions were, “remarkably effective,” according to a report of the “Copenhagen Round Table on the United Nations Sanctions in the Case of the Former Yugoslavia.” The E.U., NATO and other regional intergovernmental organizations supported these sanctions with strong international cooperation. The report concluded:

*The economic sanctions against the Federal Republic of Yugoslavia (Serbia and Montenegro), and — at a later stage — those areas of the Republic of Bosnia and Herzegovina under the control of Bosnian Serb forces, have been remarkably effective. They modified the behavior of the Serbian party to the conflict and may well have been the single most important reason for the Government in Belgrade changing its policies and accepting a negotiated peace agreement in Dayton, United States of America, in November 1995 (emphasis added).*⁶²

9. *Crack down on transshipment points.*

For enforcement to succeed, the U.S. needs to ensure that enablers at transshipment ports, such as those in the United Arab Emirates, can no longer help Iran without paying a price. To address the role of Dubai and other growing centers of transshipment like Malaysia and Hong Kong, the Obama administration should adopt the following recommendations outlined by former U.S. Treasury official Michael Jacobson.⁶³

a. Increase the number of U.S. investigators who perform physical end-use checks overseas.

As Jacobson points out, U.S. Immigration and Customs Enforcement has 63 offices spread across 45 countries. With additional support, ICE could aid the enforcement effort immensely, particularly at high-risk locations. Working with host governments, joint end-use investigation teams could conduct on-site verifications, ensuring that dual-use goods are not exported to Iran. In 1997, the U.S. and the E.U. signed a Customs Mutual

⁶² Report of the Copenhagen Round Table on United Nations Sanctions in the Case of the Former Yugoslavia, held under the auspices of the OSCE in Copenhagen, Denmark on June 24 and 25, 1996. (www.un.org/Docs/sc/committees/sanctions/s96776.pdf)

⁶³ Michael Jacobson, “Closing Loopholes: Another Vital Aspect of Sanctions on Iran,” *The Washington Institute for Near East Policy*, March 4, 2010. (<http://www.washingtoninstitute.org/templateC05.php?CID=3183>)

Assistance Agreement enabling broad sharing of information on customs-related matters. In certain locations, the E.U. may enjoy greater access than the United States.

b. The U.S and EU could work more closely together on end-use verifications.

The EU relies heavily — some would say almost exclusively — on self-reporting when it comes to verification of cargo destinations. By working more closely together, the U.S. and Europeans could strengthen their export controls and coordinate enforcement through joint U.S.- E.U. sanctions enforcements.

c. Work to strength enforcement laws of allies

Sanctions enforcement, particularly when it requires monitoring transactions abroad, can only be effective if the laws and enforcement mechanisms of our allies are as strong as they can be. The U.S. could also provide assistance to countries that seek to write stronger sanctions enforcement laws, and reward countries with more favorable trade laws or free trade agreements.

d. Transparency: the U.S. and the EU should create a Universal Database of Bad Actors

Jacobson also notes that there is no centralized database of bad actors that could help government officials and the private sector identify repeat export-control violators or identified front companies. The Brussels-based World Customs Organization, if tasked, may be an appropriate place to consider housing the database.

10. Strengthen SEC disclosure requirements for companies doing business with Iran and broaden the definition of 'material' information.

Currently, the Securities and Exchange Commission (SEC) does not require U.S. or foreign companies to specifically disclose all business dealings with designated countries such as Iran. Rather, the definition of what they must disclose — that which “constitutes material information” — is vague and translated as “information substantially likely to be significant to a reasonable investor’s decision about whether to invest in that company.”

There is too much room for interpretation and both the U.S. government and the American people deserve to know more about who is trading with Iran.

The SEC has made efforts to encourage better disclosure of business dealings with Iran, but it currently lacks the statutory authority to enforce such disclosure. Congress can help by broadening the definition of “material” information to include non-quantitative risk factors like reputational risk that may influence an investor’s decision to invest in a given company.

Last week, Congressman Ted Deutch (D-FL), supported by a bipartisan group of his colleagues, introduced legislation aimed at doing just that. The legislation, the *Iran Transparency and Accountability Act of 2010*, would force companies to disclose their business dealings with Iran so that investors can decide if they wish to invest in

companies that prop up the Iranian regime. Instead of having the SEC selectively examine companies that may report doing business with Iran, the new legislation would require all business dealings that are sanctionable to be reported and trigger an investigation.

Furthermore, the SEC would aggregate the information so that it is available to key government agencies and viewable by the public on the SEC's website. The bill would also require the President to investigate all business ties with the IRGC, its affiliates, and any Iranian banks. These disclosure requirements would give teeth to existing U.S. policy and require rigorous enforcement of legislation that has existed for decades.

Conclusion

The Iranian energy sector is the lifeblood of the regime. It is the source of its power and control over the Iranian people. The Iranian energy sector is now facing significant challenges as a result of sanctions and mismanagement. The push for energy sanctions, including steps to make it more difficult for Iran to import gasoline, acquire key energy technology, and attract investment for its energy sector, has already had a major impact. Iran's gasoline suppliers are exiting the market while energy investors, banks, technology providers, and insurers are terminating or reducing their business ties.

President Obama now has an opportunity to enforce U.S. law and put Iran's energy partners to a choice between doing business with the Iranian regime and continuing their business relationships in the lucrative U.S. market. Anything less than rigorous enforcement of U.S. sanctions laws — including stiff penalties against violators — will be a signal to these companies and the Iranian regime that Washington is prepared to allow business to continue as usual.

The options to deal with the Iranian nuclear weapons program are not between good and bad but between bad and worse. Sanctions are not a silver bullet. However, they present a peaceful alternative that could put enough pressure on Tehran to change its behavior.

On behalf of the Foundation for Defense of Democracies, I thank you for inviting me to testify before this distinguished committee.

-ENDS-