International Crisis Group
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Spider Web: The Making and Unmaking of Iran Sanctions

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Executive Summary

With war a frightening prospect and fruitful negotiations a still-distant dream, sanctions have become the West's instrument of choice vis-à-vis Iran. They are everywhere: in the financial arena, barring habitual commercial relations; in the oil sector, choking off Tehran's principal source of currency; in the insurance sector, thwarting its ability to transport goods. Without doubt, they are crippling Iran's economy. But are they succeeding? By at least one important criterion (the intensity of Western concern over nuclear progress), plainly they are not. Add to this myriad unintended consequences (bolstering the regime's ability to allocate goods; harming ordinary citizens; pushing leaders persuaded the goal is regime change to escalate its own retaliatory steps; and constructing a web of punitive measures harder to unknot than to weave). Sanctions are not necessarily counterproductive. But, too easily they become a path of least resistance, a tool whose effectiveness is assessed by the harm inflicted, not how much closer it brings the goal. In future cases, policymakers should make sure to constantly re-evaluate their effects. For now, the priority is devising a menu of meaningful, realistic sanctions relief to match meaningful, realistic nuclear concessions.

Not the product of a single policy, the sanctions regime has mutated over three decades, been imposed by a variety of actors and aimed at a wide range of objectives. The end result is an impressive set of unilateral and multilateral punitive steps targeting virtually every important sector of Iran's economy, in principle tethered to multiple policy objectives (non-proliferation; anti-terrorism; human rights) yet, in the main, aimed at confronting the Islamic Republic with a straightforward choice: either comply with international demands on the nuclear file, or suffer the harsh economic consequences.

The story of how the international community reached this point is a study in the limitations and frustrations (some unavoidable, many self-inflicted) it has faced in seeking to influence Iranian policy. It is a study in the irresistible appeal of sanctions, backed both by hardliners who wish to cripple the regime and by more moderate actors who view them as the alternative to a military strike. And it is a study in how, over time, means tend to morph into ends: in the absence of any visible shift in Tehran's political calculus, it is difficult to measure their impact through any metric other than the quantity and severity of the sanctions themselves. That they have yet to significantly curb Tehran's nuclear drive becomes, in this context, more or less an afterthought.

A key problem is that the West and Iran view the sanctions through highly dissimilar prisms. European and U.S. officials bank on a cost-benefit analysis pursuant to which the Islamic Republic, at some point, will conclude that persevering on the nuclear track will prompt economic hardships sufficiently great to trigger more extensive popular unrest, ultimately threatening regime survival itself. But the world looks very different from Tehran. There, the one thing considered more perilous than suffering from sanctions is surrendering to them; persuaded the West is intent on toppling the regime, the leadership views economic steps as just one in a panoply of measures designed to destabilise it. Its strategy, rooted in the experience of diplo-

matic isolation and the war with Iraq, can be summed up in two words: resist and survive, the former being the prerequisite to the latter.

So there are good reasons for thinking that, rather than adjusting its nuclear policy to remove the sanctions, the regime will continue to adjust its economic policy in order to adapt to them. Likewise, whatever lobbying has occurred from key domestic constituencies principally has been aimed at convincing the regime to amend its economic as opposed to its nuclear approach. Tellingly, and while important regime constituencies have been harmed by international penalties, not all of them have been harmed equally and not all of them have been harmed at all. Governmental and quasi-governmental institutions still dominate the economy, and evidence suggests that groups with superior contacts with the state have been in a position to weather the storm, circumvent sanctions, exploit new opportunities and thus minimise any damage to their interests. The net effect is to mould the nation's political economy in ways that run directly counter to the sanctioning nations' stated intent.

There are other unintended implications. The more comprehensive the sanctions, the likelier they will harm average citizens. For all the West's efforts to exempt humanitarian goods, reports of widespread shortages, notably of specialised medicine, abound. This can be attributed partly to regime inefficiency, but only partly. For sanctions, notably as comprehensive and far-reaching as those presently in effect, inevitably have both a snowballing and chilling effect. Iranians lack foreign currency. Foreign businesses, fearing they might unknowingly cross an impermissible line, prefer to shy away even from authorised deals. Transaction costs have escalated. In turn, this means that the target of public wrath is now more evenly divided between a regime viewed as incompetent and an outside world seen as uncaring.

Ultimately, sanctions as a tool of coercive diplomacy are only as effective as the prospect of relieving them in exchange for policy shifts is real; the measure of efficacy lies in what can be obtained when they are removed, not what happens when they are imposed. Therein lies another problem. For in the Iranian case, the situation at best is murky in this regard. Although long reluctant to acknowledge the impact of sanctions or project any eagerness to see them lifted, Iranian officials increasingly identify such a step as a condition for any accord. Yet that is far easier said than done. Sanctions have become so extensive and so intricately woven that it will be hard to offer significant, concrete relief short of a major – and improbable – turnaround in major aspects of the Islamic Republic's domestic and foreign policies; reaching the threshold for removing U.S. sanctions in particular is hard to imagine. That leaves the option of a time-limited suspension or waiver, which in turn is likely to prompt at best time-limited and reversible Iranian reciprocal steps.

Too, the impact of sanctions in many cases has acquired a life of its own, one that will outlast the measures themselves. This is because important trading and consumption patterns already have changed. Companies and countries that have shifted away from Iran – often at considerable expense – are unlikely to rush back, at least short of solid assurances that any decision to remove the penalties will be lasting rather than temporary.

Finally, there is another, considerable risk: that by placing all one's eggs in the sanctions basket, failure may appear to leave no other option but war.

None of this is meant to indict sanctions as a policy tool. Even in the Iranian case, it is plausible that, in their absence, Tehran might have advanced further along the nuclear path. And they remain an option preferable to military confrontation. But, at a minimum, it argues for exhibiting greater prudence and judiciousness in imposing them; resisting the impulse to pile on more sanctions when those already in place do not succeed; constantly assessing and reassessing their social and economic consequences; and preserving sufficient nimbleness so that they can be used – including through their removal – to advance negotiations in a diplomatic process where a scalpel, not a chainsaw, is required.

As far as Iran is concerned, it is too late to reverse course. The massive sanctions regime is in place, warts and all, and not about to be removed. The challenge for the P5+1 (the five permanent members of the Security Council plus Germany) is to devise a package of incentives, including some less than complete degree of relief, that is politically as well as legally achievable and that genuinely addresses Iranian concerns. And the challenge for Tehran will be to respond in kind. This week's meeting at Almaty offers the two sides an opportunity to start down that path.

Recommendations

To address the healthcare crisis in Iran

To the government of Iran:

1. Streamline currency allocation, licensing and customs procedures for medical imports.

To the government of the United States and the European Union:

2. Provide clear guidelines to financial institutions indicating that humanitarian trade is permissible and will not be punished.
3. Consider allowing an international agency to play the role of intermediary for procuring specialised medicine for Iran.

To sustain nuclear diplomacy and bolster chances of success

To the P5+1 [permanent UN Security Council members and Germany] and the government of Iran:

4. Agree to hold intensive, continuous, technical-level negotiations to achieve a step-by-step agreement and, to that end, consider establishing a Vienna- or Istanbul-based contact group for regular interaction.
5. Recognise both Iran's right in principle to enrich uranium for peaceful purposes on its soil and its obligation to provide strong guarantees that the program will remain peaceful.

To the governments of Iran and the United States:

6. Conduct bilateral negotiations on the margins of the P5+1 meetings or parallel to them.

To address the immediate issue of 20 per cent uranium enrichment

To the P5+1 and the government of Iran:

7. Seek agreement on a package pursuant to which:
   a) Iran would suspend its uranium enrichment at 20 per cent level for an initial period of 180 days and convert its existing stockpile of 20 per cent enriched uranium to nuclear fuel rods; and
   b) P5+1 members would provide Iran with medical isotopes; freeze the imposition of any new sanctions; waive or suspend some existing sanctions for an initial period of 180 days (eg, the ban on the sale of precious and semi-finished metals to Iran or the prohibition on repatriating revenues from Iranian oil sales); and release some of Iran's frozen assets.

To address the issue of Fordow

To the P5+1 and the government of Iran:

8. Seek agreement on a package pursuant to which:
   a) Iran would refrain from installing more sophisticated Centrifuges at Fordow and implement additional transparency measures, such as using the facility exclusively for research and development purposes and allowing in-house International Atomic Energy Agency (IAEA) resident inspectors or installing live-stream remote camera surveillance; and
   b) P5+1 members would suspend sanctions affecting Iran's petro-chemical sector or permit Iran's oil customers to maintain existing levels of petroleum imports.

To reach a longer-term agreement

To the P5+1 and the government of Iran:

9. Seek agreement on a package pursuant to which:
   a) Iran would limit the volume of stockpiled 5 per cent enriched uranium, with any amount in excess to be converted into fuel rods; ratify the IAEA's Additional Protocol and implement Code 3.1; and resolve outstanding issues with the IAEA; and
   b) P5+1 members would provide Iran with modern nuclear fuel manufacturing technologies; roll back financial restrictions; and lift sanctions imposed on oil exports; the P5 would submit and sponsor a new UN Security Council resolution removing international sanctions once issues with the IAEA have been resolved.

To rationalise future resort to sanctions on third countries

To the U.S. and European Union:

10. Consider setting up an independent mechanism to closely assess, monitor and re-evaluate the social and economic consequences of sanctions both before and during implementation to avoid unintended effects, harming the general public or being trapped in a dynamic of escalatory punitive measures.
11. Avoid where possible imposition of multi-purpose sanctions lacking a single strategic objective and exit strategy.

Washington/Brussels, 25 February 2013

Spider Web: The Making and Unmaking of Iran Sanctions

I. Introduction

At the centre of efforts to resolve the nuclear standoff between Iran and the West has been the imposition of ever-tightening economic sanctions, hailed by the U.S. and Europe as the most comprehensive ever enacted. Perceptions differ widely. For many Western officials, they are the key to pressuring Tehran to compromise without resorting to military force.[1] Iranian leaders, while more recently acknowledging their punishing economic impact, reject the notion that sanctions will produce concessions and – particularly in light of other coercive policies, such as assassination of Iran's nuclear scientists, sabotage and cyber-attacks – see them as evidence that the West's true goal is regime rather than behaviour change.[2]

Even now, as (meagre) hopes revive for resumed negotiations between the P5+1 (permanent Security Council members in addition to Germany) and Iran, the issue of sanctions looms large. In the wake of his re-election, U.S. President Barack Obama made a direct linkage:

> We've imposed the toughest sanctions in history. It is having an impact on Iran's economy. There should be a way in which they can enjoy peaceful nuclear power while still meeting their international obligations and providing clear assurances to the international community that they're not pursuing a nuclear weapon.[3]

In response, Iran's Supreme Leader – even as he denied pursuit of a nuclear weapon – emphatically rejected any link between economic hardship and nuclear policy:

[1] A former U.S. official said, "there are three views on what the sanctions are supposed to achieve: (1) persuade the Iranian side to negotiate seriously over the nuclear issue (the official Western position); (2) bring enough pressure to bear so that the Iranians capitulate; and (3) force the regime to collapse under economic hardship. If you listen to enough policymakers in Washington and Brussels, you can hear all three views". Crisis Group interview, Washington, 15 February 2013.

[2] For a review of the more recent rounds of discussion, see Crisis Group Middle East Briefing N°34, *The P5+1, Iran and the Perils of Nuclear Brinkmanship*, 15 June 2012. For an extensive review of the Iranian nuclear crisis, see earlier Crisis Group reporting, in particular, Crisis Group Middle East and Europe Report N°116, *In Heavy Waters: Iran's Nuclear Program, The Risk of War and Lessons from Turkey*, 23 February 2012; Asia Briefing N°100, *The Iran Nuclear Issue: The View from Beijing*, 17 February 2010; Middle East Report N°51, *Iran: Is There a Way Out of the Nuclear Impasse?*, 23 February 2006; and Middle East Report N°18, *Dealing with Iran's Nuclear Program*, 27 October 2003.

[3] He continued: "I very much want to see a diplomatic resolution to the problem. I was very clear before the campaign, I was clear during the campaign, and I'm now clear after the campaign – we're not going to let Iran get a nuclear weapon. But I think there is still a window of time for us to resolve this diplomatically …. I think it's fair to say we want to get this resolved, and we're not going to be constrained by diplomatic niceties or protocols. If Iran is serious about wanting to resolve this, they'll be in a position to resolve it". Quote from "Remarks by the President in a News Conference", The White House, 14 November 2012.

> You impose – in your own words – crippling sanctions to paralyse the nation. Does this show good or ill intention. … They naïvely think that the nation has been exhausted by the sanctions and will therefore yearn for negotiations with the U.S.[4]

Other Iranian officials expressed puzzlement that Obama's statements had been accompanied by new legislation further tightening the noose.[5] One said:

> Words matter, but political will matters more; and there is no sign of the latter in Washington when it gets to serious engagement with Iran. That the White House cannot convince the dozen hawks in Congress to give diplomacy a real chance signals more of the same contradictory dual-track policy of pressure and persuasion.[6]

How effective sanctions can be in affecting fundamental Iranian policy choices is one important area of inquiry. At one level, its leaders appear confident they can ride the storm, having endured far more devastating conditions in the past, notably during the eight-year war with Iraq.[7] Beyond that, sanctions could be strangulating Iran's economy, and Tehran's leaders might be willing to pay a tactical price for their removal without this necessarily establishing that Iran's basic goals will have changed. Iran's economy without question is under tremendous strain, having suffered a dramatic drop in oil exports and a no less significant collapse in the value of its currency.

But evidence of a concomitant impact on Tehran's policy choices is far less easy to detect. To this, there are several possible, non-mutually exclusive explanations. First, the Iranian system might be relatively impervious to political manifestations (in terms of popular discontent or anger of the business community) of even sharp economic distress.[8] Secondly, the regime harbours the strong conviction that any policy change would signal weakness and thus, rather than lessen pressure would be likely to augment it;[9] hence its leadership's determination to prove that, although "sanctions might affect Iran, they never will yield the desired result".[10] As a European

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[4] Quoted in *The New York Times*, 17 February 2013.

[5] On 2 January 2013, President Obama signed the National Defense Authorization Act (NDAA) of 2013, which includes extraterritorial U.S. sanctions targeting Iran's energy, insurance, shipping and shipbuilding sectors and bans supply of precious metals to Iran. See, NDAA of 2013, Subtitle D – Iran Freedom and Counter-Proliferation Act of 2012.

[6] Crisis Group interview, Iranian official, December 2012.

[7] Iran's leaders have decades of experience in surviving sanctions and many believe they can sustain more of the same. A chamber of commerce member said, "the Iranian economy is like a bird whose wings have been clipped. It can no longer fly, but it can still walk. A millenary culture of entrepreneurship, abundant resources, and porous borders have and will continue to help the Iranian economy stay afloat". Crisis Group telephone interview, Tehran, August 2012.

[8] Iranian businessmen complained that, as they had no channel for communicating their grievances to the government, they preferred to keep quiet. Crisis Group interviews, Dubai, Istanbul, April, August 2012. The general public, notwithstanding widespread disgruntlement, appears largely quiescent. An Iranian political analyst said, "Iranians are not seeking radical change. The regional situation and our own recent revolutionary experience are sufficient reminders that the line between tyranny and anarchy is a narrow one". Crisis Group telephone interview, Tehran, June 2012.

[9] "It is obvious that sanctions are aimed at regime change. They were in place before the nuclear crisis, and they will remain in place after it. Iran will never be off the hook, as there always will be other pretexts such as human rights or regional issues". Crisis Group interview, Iranian official, October 2012.

[10] According to a member of Iran's nuclear negotiating team, "during the past decade, especially in the past seven years, Iran has tried to come up with a model of security strategy whose main goal is to disprove the fundamental premise of the dual-track strategy [pressure and engagement]. Iran wants, and has been able, to prove that the path of pressure will not provide support for the path of

official put it, "Iran's strategy now boils down to 'resistance till victory', which stands in sharp contrast to the West's 'sanctions till victory'".[11]

Even assuming their efficiency as a political instrument, the second question concerns the practicality of their use: imposing sanctions in order to modify behaviour is only useful if they can be removed in response to altered practice in a calibrated, flexible way. Without such nimbleness, the West will be unable to offer Iran necessary incentives. The real measure of efficacy is not sanctions imposition. It is sanctions relief.

This is no straightforward matter. More than three decades after the first U.S. sanctions, a complex set of UN and multilateral measures have given rise to a multilayered architecture whose undoing will be at least as complex as its making. The diversity of objectives coupled with the multiplicity of sanctioning parties, each with different legal frameworks and implementing bodies, increasingly has turned sanctions into a blunt tool, hampering the agility required by subtle diplomatic moves. A sanctions expert said, "easing the sanctions is like dancing in a minefield. There are tripwires everywhere".[12]

Gauging the impact of sanctions also requires taking account of potential unintended consequences. Shortages of food and vital medicine, eerie reminders of Iraq's conditions during the late 1990s, are on the rise.[13] Many citizens may well share Nobel Peace Laureate Shirin Ebadi's sentiments – namely, that "the government's mismanagement and endemic corruption are more at blame for the country's woes than economic sanctions".[14] The impact of those sanctions is nevertheless undeniable, and this is costing the West a share of good-will on Iran's streets.[15] Indeed there are indications that the more recent severe humanitarian hardships have begun to tilt popular allocation of responsibility for Iran's predicament towards the West.[16]

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negotiation". See Mehdi Mohammadi, "2013، بن بست یا گشایش؟" ["2013, Breakdown or Breakthrough?"], *Vatan Emrooz*, 1 January 2013.

[11] Crisis Group interview, Brussels, September 2012.

[12] Crisis Group interview, Washington, December 2012.

[13] For an overview of how sanctions have impeded medicine and food supply, see Julian Borger and Saeed Kamali Dehghan, "Iran unable to get life-saving drugs due to international sanctions", *The Guardian*, 13 January 2013; Jonathan Saul and Marcus George, "Sanctions side effect hits Iran's food system", Reuters, 28 November 2012.

[14] Crisis Group interview, London, 24 December 2012. An Iranian business consultant noted: "No doubt the Iranian government's mismanagement and general unpreparedness, along with myriad other deficiencies in the country's pharmaceutical sector, compounded and exacerbated this complex problem. Yet there is no mistaking that the shortages of medicine and medical equipment started with the sanctions. Iran had the same government with the same 'talented mismanagement' before the sanctions, and there was plenty of medicine and food". Crisis Group interview, Siamak Namazi, general manager, Access Consulting Group, Dubai, 21 December 2012.

[15] Western officials still maintain that their sanctions are targeted towards Iran's decision-makers and not its citizenry and put the blame squarely on Tehran. John Sullivan, a U.S. treasury spokesman, said, "if there is in fact a shortage of some medicines in Iran, it is due to choices made by the Iranian government, not the U.S. government". Quoted in Borger and Dehghan, "Iran unable to get life-saving drugs", op. cit. Some Western officials suggest Iran has been exaggerating the medical crisis. See Farideh Farhi, "Who is Responsible for Medicine Shortages in Iran?", Lobelog.com, 21 January 2013.

[16] According to a recent Gallup poll, 47 per cent of Iranians blame the U.S. for their hardships, as opposed to 10 per cent who hold their own government responsible. Such polling is inherently unreliable, of course, especially in closed societies and thus must be taken with a grain of salt. See Mohamed Younis, "Iranians Feel Bite of Sanctions, Blame U.S., Not Own Leaders", Gallup.com, 7 February 2013.

A prominent Iranian entrepreneur said, "it is truly mindboggling that the West has levied its most draconian sanctions against the most pro-Western nation in the Middle East".[17]

The effectiveness of sanctions as an instrument of coercive statecraft has been fiercely debated among policymakers, observers and academics. Although there is some consensus regarding the circumstances under which economic pressure is likely to elicit positive change – eg, when it is imposed multilaterally; in pursuit of modest and specific objectives; and targeted at more democratic states – there are fundamental disagreements about their overall efficacy.[18] As one of the most – if not the most – sanctioned country in the world, Iran offers a significant, real-life and (considering the likely alternative to success) high-risk case study.[19]

This report aims to analyse both the origins and scope of sanctions imposed on Iran but also to use this specific instance to offer broader lessons for the general sanctions debate.

[17] Crisis Group interview, Istanbul, August 2012.
[18] For arguments on both sides of the sanctions debate, see "Designing United Nations Targeted Sanctions", Targeted Sanctions Consortium, August 2012; Robert A. Pape, "Why Economic Sanctions Still Do Not Work," International Security, vol. 23, no. 1 (summer 1998), pp. 66-77; George Lopez and David Cortright, "Containing Iraq: Sanctions Worked", *Foreign Affairs*, vol. 83, no. 4 (July/August 2004), pp. 1-14; Joy Gordon, "Smart Sanctions Revisited", *Ethics & International Affairs*, vol. 25, no. 3 (September 2011), pp. 315-335; George Lopez, "In Defense of Smart Sanctions: A Response to Joy Gordon", ibid, vol. 26, no. 1 (March 2012), pp. 135-146.
[19] Sanctions experts reviewing cases from the second half of the twentieth century have concluded that in over 60 per cent of cases involving the U.S., sanctions were a prelude to military conflict. See Monika Klimek and Jerome Venteicher, "Where Does Diplomacy End? The Turning of the Screw from U.S. Economic Sanctions to Military Dispute", International Studies Association, Chicago, 1 March 2007.

II. Weaving the Net

Since it was established in 1979, the Islamic Republic of Iran has been subjected to a steady stream of sanctions. Over the years, their depth and breadth has dramatically increased, often gradually, at times by leaps and bounds. The existing patchwork of sanctions reflects diverse policy objectives and disparate legal frameworks, developed and evolved over 34 years and implemented by different governmental and institutional bodies.

Unilateral U.S. sanctions, first imposed in the 1980s, eventually morphed into what is now a broad, international regime. The first wave (1979 to 1995) originated as a U.S. response to the embassy hostage crisis, Tehran's more broadly anti-American policies and its support for violent groups. The second (1995 to 2006), also unilaterally enforced by Washington, had several purposes: weaken the regime by targeting its oil and gas industry and denying it access to dangerous nuclear and missile technology, while also – through extraterritorial applicability of third-party sanctions – compelling U.S. allies to adopt a unified stand. The third wave (2006 to 2010) comprised both multilateral and international targeted punitive measures propelled by concerns over Iran's nuclear ambitions. Their failure to resolve the standoff broke open the floodgates, eventually giving rise to yet another wave, this time involving ever harsher unilateral and coordinated multilateral comprehensive sanctions (2010 to present).

A. *Unilateral U.S. Sanctions*

A turning point in U.S.-Iranian relations occurred on 4 November 1979, when American diplomats were taken hostage in Tehran. The Carter administration responded in part by banning the import of Iranian crude oil.[20] Over the course of the following, tension-packed months, a string of Executive Orders (EOs) froze $12 billion worth of Iranian government assets within U.S. jurisdiction,[21] barred exports of U.S. goods to Iran; severely restricted financial transactions with the country;[22] banned all Iranian imports; and prohibited U.S. citizens from travelling to and conducting business with Iran.[23]

All these measures – with the exception of the assets freeze, which remains a point of contention between the two nations – were revoked by President Ronald Reagan, after the hostages were released on his inauguration day.[24] Yet, a few years later, in January 1984, sanctions were re-imposed, when the State Department designated

[20] Proclamation 4702, Imports of Petroleum and Petroleum Products From Iran, 12 November 1979. A detailed listing and analysis of all main U.S., EU and UN sanctions are contained in Appendices A and B below and on www.crisisgroup.org.
[21] Executive Order 12170, Blocking Iranian Government property, 14 November 1979. Unlike an act of Congress, an executive order can be unilaterally repealed by the president.
[22] Executive Order 12205, Prohibiting certain transactions with Iran, 7 April 1980. Food, medicine and humanitarian aid were exempted.
[23] Executive Order 12211, Further prohibitions on transactions with Iran, 17 April 1980. The Treasury's Office of Foreign Assets Control (OFAC) is in charge of administering and enforcing U.S. sanctions.
[24] Executive Order 12282, Revocation of prohibitions against transactions involving Iran, 23 January 1981. Removal of "all sanctions" was one of the conditions of the Algiers Accords, signed between Iran and the U.S. on 19 January 1981. Both countries agreed to end litigation between their respective governments and citizens, referring the cases to international arbitration at the Iran-United States Claims Tribunal, which continues its work in The Hague.

Iran as a state sponsor of terrorism for its alleged involvement in the 1983 bombing of U.S. marine barracks in Beirut.[25] The designation denied Iran, in the midst of its war with Iraq, access to financial aid, dual-use technology and U.S. defence exports.[26]

In August 1986, Congress passed the Arms Export Act, barring Iran from receiving U.S. arms and spare parts.[27] The following year, invoking continued Iranian aggression against U.S. flagged vessels in the Persian Gulf and Tehran's purported support for terrorism, the president issued an executive order banning all imports of Iranian crude oil, goods and services.[28]

In the wake of the Iran-Iraq War, which ended in 1988, Washington sought to blunt Tehran's efforts to reconstitute its conventional military capability. In 1992, Congress passed the Iran-Iraq Arms Nonproliferation Act, prohibiting sales of conventional and unconventional weapons to Iran.[29] Pointing to its support for violent movements in the Levant, primarily Hizbollah and the Palestinian Islamic Jihad, as well as its signing of a contract with Russia to complete the Bushehr nuclear power plant,[30] the Clinton administration took more punitive steps. In 1995, it proscribed all U.S. investment in Iran's oil and gas sectors[31] and, subsequently, all involvement

[25] The designation entails a ban on direct U.S. financial assistance and requires U.S. representatives in multilateral organisations to vote against any lending; it also bans exports of arms and dual-use items. These triggers are contained in separate laws, namely the Export Administration Act, the Arms Export Control Act and the Anti-Terrorism and Effective Death Penalty Act, which apply the provisions to any country on the terrorism list. For a detailed account of the 1983 Beirut bombing, see David Crist, *The Twilight War: The Secret History of America's Thirty-Year Conflict with Iran* (New York, 2012), pp. 139-159. To date, U.S. federal courts in eight separate judgments have awarded a total of $8.8 billion to families of the 241 killed U.S. soldiers. See Agence France-Presse, 6 July 2012.

[26] The president's authority to remove a country from the terrorism list is subject to Congressional approval after a 45-day notification period. Rescission of the designation would require the president to certify to Congress that Iran has not provided support for acts of terrorism within the preceding six months and has provided assurances that it will not support acts of international terrorism in the future. Congress can block the removal by enacting a joint resolution of opposition, subject to presidential veto, itself subject to override by a two-thirds supermajority. In 2008, North Korea was removed from the terrorism list in exchange for cooperation on its nuclear program. Libya was removed from the list in 2006.

[27] A few months later, the administration violated the embargo by secretly facilitating the sale of arms to Iran in exchange for the release of U.S. hostages held in Lebanon. For more information on the so-called Iran Contra Affair, see Lawrence E. Walsh, "Final report of the independent counsel for Iran/Contra matters", United States Court of Appeals for the District of Columbia Circuit, 4 August 1993.

[28] Executive Order 12613, Prohibiting imports from Iran, 29 October 1987.

[29] Iran-Iraq Arms Nonproliferation Act, Title XVI of the National Defense Authorization Act for Fiscal Year 1993, Public Law: 102-484, 23 October 1992. The Act imposed sanctions on foreign entities that supply Iran with "destabilizing numbers and types" of conventional weapons or Weapons of Mass Destruction (WMD). Violations result in suspension of U.S. assistance, technical exchange, coproduction agreements and sales of U.S. arms to the incriminated country for a period of one year. U.S. representatives also are required to vote against international lending to that country for a period of one year. The president can exercise his waiver authority fifteen days after he determines and reports to the Congress that such an undertaking is essential to U.S. national interests. The International Emergency Economic Powers Act (IEEPA) provides other tools for the president to regulate commerce with a country that defies U.S. laws.

[30] "Iran, Russia Agree on $800 Million Nuclear Plant Deal", *The Washington Post*, 9 January 1995.

[31] Announcing that "the actions of the government of Iran pose an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States", President Clinton declared a state of emergency between the two nations on 15 March 1995. Since then, every administration

by U.S. firms in developing, or helping to develop Iran's oil industry.[32] Shortly thereafter, an executive order barred all U.S. trade with and investment in Iran,[33] as well as re-export by third countries of U.S. products to Iran.[34]

Aware that without cutting off third-party exchanges with Iran, U.S. sanctions would have only limited effect, Washington focused on the extraterritorial reach of its measures. Enacted in August 1996, the Iran-Libya Sanctions Act (later renamed Iran Sanctions Act, ISA) was the first dramatic example of efforts to deter foreign companies from investing in Iran's energy sector.[35] European countries vehemently opposed these secondary sanctions, both as a matter of principle and because they were engaged in a process of "critical dialogue" with Tehran at the time.[36] The European Union (EU) prohibited its firms from complying with ISA,[37] and the standoff nearly sparked a transatlantic commercial trade war.[38] This was averted after the

has extended the status on an annual basis. Earlier that month, Conoco, a U.S. oil company, had signed a $1 billion contract with Iran to develop its oil and gas fields. See Paul Richter and Robin Wright, "Clinton Kills Pending Iran-Conoco Oil Deal", *Los Angeles Times*, 15 March 1995.

[32] Executive Order 12957, Prohibiting Certain Transactions With Respect to the Development of Iranian Petroleum Resources, 15 March 1995.

[33] Executive Order 12959, Prohibiting Certain Transactions With Respect to Iran, 6 May 1995. Ironically, the period preceding the embargo had witnessed a sharp rise in trade between Iran and the U.S. The U.S. had become Iran's sixth largest source of imports, with nearly $2.2 billion worth of trade from 1991 through 1994.

[34] Executive Order 13059, Prohibiting Certain Transactions With Respect to Iran, 19 August 1997. Items with more than 10 per cent U.S. content are considered by law as U.S. products. The president may terminate such sanctions, in whole or in part, if the president notifies Congress at least fifteen days in advance of such termination. EOs 12957, 19959 and 13059 subsequently were codified in the Iran Freedom Support Act of 2006; as a result the president no longer can unilaterally end or amend the trade ban.

[35] Iran Sanctions Act, Public Law 104-172, 6 August 1996. The bill passed in the House of Representatives with no opposing vote and the Senate with unanimous consent. The Libya component of the Act was terminated in 2004. Over the years, legislation expanded the triggers and sanctions under ISA while circumscribing presidential waiver authority. Whereas the original trigger was established at $20 million investment in Iran's oil sector, the current list of triggers ranges from selling gasoline to Iran, to investing in Iran's petrochemical sector and providing insurance for Iranian oil tankers. See Kenneth Katzman, "Iran Sanctions", Congressional Research Service, 10 January 2013. In order to terminate sanctions under ISA, the president must certify that Iran has ceased efforts to design, develop or acquire nuclear, chemical and biological weapons, as well as ballistic missile technology; has been removed from the U.S. list of state sponsors of terrorism; and poses no significant threat to U.S. national security interests or its allies. ISA is scheduled to expire, unless extended, on 31 December 2016.

[36] For a review of the "critical dialogue" between Iran and Europe see, Bernd Kaussler, "From Engagement to Containment: EU-Iran Relations and the Nuclear Programme, 1992-2011", *Journal of Balkan and Near Eastern Studies*, vol. 14, no. 1, March 2012, pp. 53-76.

[37] Council Regulation (EC), no. 2271/96, Protecting against the effects of the extra-territorial application of legislation adopted by a third country, and actions based thereon or resulting therefrom, 22 November 1996.

[38] At the time, the French foreign ministry spokesman, Yves Doutriaux, asked: "Is one nation telling the rest on earth what they can and can't do. Is that right?" The first serious challenge to the bill was made by the French oil company Total SA, which, along with minority partners Gazprom of Russia and Pertronas of Malaysia, signed a $2 billion contract to develop phases two and three of the massive South Pars gas field. See Adrian Croft, "EU warns of WTO move if U.S. imposes sanctions", Reuters, 27 May 1998.

U.S. exempted European companies in return for increased cooperation on counter-terrorism and non-proliferation issues.[39]

Mohammad Khatami's upset victory in the 1997 presidential elections, which appeared to signal a softening of Iran's policies, briefly led to a relaxation of sanctions. In 1999, President Clinton used his waiver power to authorise the sale of medicine and food to Iran and again in 2000 to enable the import of pistachios, carpets and caviar from that country.[40] Yet, increased U.S. concern over Iranian-Russian nuclear cooperation quickly closed the parenthesis. In 2000, Congress passed the Iran Non-proliferation Act, ordering sanctions on foreign entities assisting Iran in developing weapons of mass destruction (WMD) and its ballistic missile programs.[41]

During George W. Bush's presidency, attention shifted squarely to the nuclear file. After Iran's covert uranium enrichment activities were brought to light in 2002, the EU-3 (France, the UK and Germany) engaged in a partially successful diplomatic effort with Tehran. The two sides reached an agreement pursuant to which Iran suspended enrichment and allowed intrusive inspection of its sites through implementation of the International Atomic Energy Agency (IAEA) Additional Protocol. In return, the EU-3 promised economic and energy cooperation.[42] Notwithstanding these negotiations, a new set of U.S. sanctions in June 2005 blacklisted individuals and entities supporting Iran's nuclear and missile programs.[43]

By January 2006, unable to bridge differences between the two sides, the EU-3's diplomatic initiative ended in failure; Iran resumed its uranium enrichment activities, and subsequently the IAEA referred the situation to the UN Security Council.[44] That year, the U.S. Congress, partly in response to reports that Iran was making progress in its nuclear program, passed the Iran Freedom Support Act (IFSA). It codified previous executive orders banning investment in and imports from Iran; it also made promotion of Iranian democracy official U.S. policy.[45] But the most significant innovation was the decision to turn to financial sanctions as a complement to more

[39] "Report to the Congress, Iran and Libya Sanctions Act: Decision to waive imposition of sanctions on firms Total, Gasprom, and Petronas for activities found sanctionable under the Act", U.S. Department of State, Washington, 1998.
[40] Katzman, "Iran Sanctions", op. cit.
[41] Special waivers were built in to allow continued cooperation between the National Aeronautics and Space Administration (NASA) and the Russian space agency. See Iran Nonproliferation Act of 2000, Public Law 106–178, 14 March 2000.
[42] Crisis Group interview, Hossein Mousavian, former Iranian nuclear negotiator, Washington, 29 August 2012.
[43] Executive Order 13382, Blocking Property of Weapons of Mass Destruction Proliferators and Their Supporters, 28 June 2005. Entities designated by this order included the Atomic Energy Organisation of Iran, the Aerospace Industries Organisation and numerous Iranian banks. The designation of the Islamic Revolutionary Guards Corps (IRGC) under this order constituted the first time that the U.S. sanctioned part of another country's military forces. For a complete list, see www.state.gov/t/isn/c22080.htm.
[44] Crisis Group Report, *Iran: Is There a Way Out of the Nuclear Impasse?*, op. cit.
[45] The Iran Freedom Support Act, Public Law: 109-293, September 30, 2006. IFSA prohibits the sale of WMD technology or destabilising numbers and types of advanced conventional weapons to Iran. The Act allocates "sums as may be necessary" to assist Iranians who officially oppose the use of violence and terrorism; advocate Iran's adherence to the nonproliferation regime; are dedicated to democratic values and respect for human rights; support fundamental freedoms; work to establish equality of opportunity; and support adoption of a democratic form of government.

traditional measures Tehran had appeared able to circumvent.[46] The U.S. Treasury Department began blacklisting major Iranian banks, pressuring and cajoling other states to follow suit.[47] Senior U.S. officials travelled the world, presenting evidence of the Iranian financial system's ties with Hizbollah, Hamas and Islamic Jihad, highlighting the reputational risks of working with banks engaged in illicit financial conduct and warning of severe penalties. With many financial institutions worldwide halting their business with Iran and the U.S. barring Iranian banks from dealing in dollars, Iran virtually became a financial pariah.[48]

Barack Obama's 2008 election appeared to herald a greater emphasis on engagement in Washington's approach toward Iran. Still, the two-track policy remained at the core, the belief being that a good-faith invitation to dialogue needed to be complemented by continued, and even sharpened pressure, if it were to produce results. This was seen as all the more relevant after Tehran appeared to spurn the first U.S. entreaties. Moreover, an upshot of the administration's outreach efforts was to bolster global support for sanctions; the good-will earned by U.S. offers of dialogue – particularly after the tumultuous Bush years – could be translated into greater multilateral coordination.

Accordingly, between 2009 and 2012, the U.S. both toughened its own pressure and turned to the UN Security Council for additional measures. Partly in response to developments such as Iran's post-2009 presidential election crackdown and failure of an effort to swap a portion of Iran's stockpile of enriched uranium for nuclear fuel rods,[49] partly under congressional pressure, the administration devised ever more

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[46] Section 311 of the Patriot Act, enacted in the wake of the 11 September 2001 terror attacks on the U.S., authorises the Treasury Department to deny entities exposed or involved in money laundering or terror financing access to the U.S. financial system. In September 2005 the Treasury Department designated Banco Delta Asia (BDA), a small Macanese bank holding North Korean assets, as an institution of money laundering concern. The designation shocked Pyongyang, arguably catalysed the 2007 agreement at Six-Party talks and inspired similar measures against Iran. See Richard S. Tracey, "Using the Patriot Act to Turn North Korea's Dirty Money into a Bargaining Chip", *Strategic Studies Quarterly* (summer 2009), pp. 124-140. In January 2006, Stuart Levey, the Under Secretary for Terrorism and Financial Intelligence at the U.S. Treasury Department, replicated the policy against Iran and spearheaded a global effort to press the private sector to curb business with Tehran. A former Iranian finance minister, Davoud Danesh-Jaffari, characterized Levey's undertaking as "a serious and breath-taking game of chess". A U.S. official said, "it's the most direct and aggressive stuff we've got going. It delivers". See Robin Wright, "Stuart Levey's War", *The New York Times*, 31 October 2008.

[47] Several international organisations, such as The Financial Action Task Force (FATF, the financial watchdog for the 34 largest economies) and the Organization for Economic Cooperation and Development (OECD, which includes 30 of the world's richest nations), warned against dealing with Iranian financial institutions. See Louis Charbonneau, "Iran bank hit hard by U.N. sanctions: diplomats", Reuters, 30 July 2007.

[48] Crisis Group interview, U.S. officials, Washington, December 2012. Prior to 2008, U.S. banks could clear indirect dollar transactions for Iranian financial institutions, an authorisation known as the 'U-turn' exception. In 2006, the U.S. Treasury Department accused one of Iran's largest banks, Bank Saderat, of facilitating fund transfers to Hizbollah and barred it from using the U.S. banking system. Two years later, the ban was extended to all other Iranian banks. This primarily affected Iran's oil receipts, as the dollar is the international currency for oil markets, and most of Iran's oil income was channelled through the U.S. financial system. See "Revoking an authorization previously granted to U.S. depository institutions to process U-turn transfers", U.S. Treasury Department, 6 November 2008.

[49] On U.S.-Iranian relations during President Obama's first-term and the nuclear fuel swap initiative, see Trita Parsi, *A Single Roll of the Dice: Obama's Diplomacy with Iran* (New Haven, 2012).

comprehensive economic penalties. These culminated in 2010 in adoption of the Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA), which targeted individuals and entities aiding Iran in developing its energy sector, took aim at Tehran's ability to import petrol and restricted its ability to engage in financial transactions.[50]

Over time, the administration issued executive orders to penalise Iranian officials for their suspected role in nuclear and missile programs; human rights abuses;[51] and alleged financial and operational assistance to the Syrian regime in suppressing anti-government protests.[52] An IAEA report in late 2011 detailing the possible military dimension of Iran's nuclear program added to the momentum for more pressure.[53] Targets included Iran's petrochemical industry and, again, persons tied to its missile and nuclear programs;[54] Washington also took banking restrictions to a new level, labelling the entire Iranian financial sector – including its Central Bank (CBI) – a "jurisdiction of primary money laundering concern".[55] Significantly, on 31 December

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[50] Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA), Public Law: 111-195, 1 July 2010. CISADA banned the sale of gasoline, related aviation fuel and other fuels to Iran and barred foreign banks conducting transactions with blacklisted Iranian institutions from access to the U.S. market. It also imposed travel bans and asset freezes on Iranians determined to have violated human rights and proscribed the sale of technology liable to be used to monitor or control the internet. CISADA includes a "special rule" pursuant to which firms that pledge to verifiably end their business with Iran and forgo any future contracts with the country are exempted from sanctions. If he deems it to be in the national interest, the president can exempt the export of some goods, services or technologies. CISADA's amendments to ISA will be terminated should the president determine that Iran no longer satisfies the requirements for designation as a state sponsor of terrorism and has ceased pursuing WMD. Termination of the act's human rights-related sanctions requires Iran to unconditionally release all political prisoners; conduct a transparent investigation into the killings, arrests, and abuse of 2009 protestors; cease human rights violations; and establish an independent judiciary.

[51] Executive Order 13553 – Blocking Property of Certain Persons With Respect to Serious Human Rights Abuses by the Government of Iran and Taking Certain Other Actions, 29 September 2010. The order impounded U.S.-based assets of eight Iranian officials and banned their entry into the country. The list included Mohammad Ali Jafari, Commander of the IRGC, Heydar Moslehi, intelligence minister, and Saeed Mortazavi, former prosecutor-general. The order was considered of symbolic value, as the listed officials were unlikely to have any assets in the U.S. Subsequently, the U.S., UK and Canada also blacklisted several other Iranian officials. See Saeed Kamali Dehghan, "Iranian officials put on travel blacklist by UK, US and Canada", *The Guardian*, 8 July 2011.

[52] Executive Order 13572 Blocking Property of Certain Persons With Respect to Human Rights Abuses in Syria, 29 April 2011. The Order mainly targeted the Quds force, IRGC's arm dealing with foreign operations, and its commander, Qassem Soleimani. Previously, in 2007, the Bush administration had imposed similar sanctions on Quds force officers accused of destabilising Iraq. See Executive Order 13438 – Blocking Property of Certain Persons Who Threaten Stabilization Efforts in Iraq, 17 July 2007.

[53] "Implementation of the NPT Safeguards Agreement and relevant provisions of Security Council resolutions in the Islamic Republic of Iran", IAEA, GOV/2011/65, 8 November 2011.

[54] Executive Order 1357 Concerning Further Sanctions on Iran, 23 May 2011, authorised implementation of financial sanctions outlined in ISA, while Executive Order 13590, Iran Sanctions, 21 November 2011, extended the list of sanctioned individuals to those knowingly engaged in the country's energy and petrochemical sectors.

[55] The action was taken under Section 311 of the USA Patriot Act. The designation was a stark warning about the risks of dealing with Iran's financial institutions – including the Central Bank of Iran. See "Fact Sheet: New Sanctions on Iran", U.S. Treasury Department, 21 November 2011. U.S. officials contend that the designations were justified, because the Central Bank was helping other Iranian banks circumvent sanctions. Crisis Group interview, Washington, December 2012.

2011, under Congressional pressure and after obtaining flexibility for incremental implementation to mitigate any impact on global energy prices, Obama signed the National Defense Authorization Act of 2012 (NDAA 2012), section 1245 of which bars foreign banks from processing oil receipts through the CBI, with the goal of gradually depleting Iran's revenues.[56]

Equally important, the administration ordered domestic financial institutions to impound all remaining Iranian governmental assets[57] and sanctioned any third-country purchase of Iranian oil and petroleum products, save for countries already exempted under the National Defense Authorization Act of 2012.[58] Expressing frustration at what it considered continued Iranian defiance, on 1 August 2012 Congress passed the Iran Threat Reduction and Syria Human Rights Act (TRA or ITRSHRA), which codified several previous executive orders; expanded both the list of sanctionable activities and attendant penalties; banned the provision of messaging services for conducting financial transactions and shipping insurance; and prohibited repatriation of Iran's oil receipts.[59]

Despite purported White House objections – based on concern that it "threaten[ed] to undercut and confuse" other sanctions – 2012 concluded with adoption of yet another harsh measure, the Iran Freedom and Counter-Proliferation Act of 2012 (IFCPA).[60] It blacklists the entire energy, shipping, shipbuilding and port operating

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[56] The measures were attached to the defence appropriation bill. The administration initially was reluctant to take this step aimed at crippling Iran's oil sales for fear it could prompt a spike in global oil prices. See Josh Rogin, "Menendez livid at Obama team's push to shelve Iran sanctions amendment", *Foreign Policy* (online), 1 December 2011. David Cohen, under secretary for terrorism and financial intelligence, testified to the Senate on 1 December 2011 that "[it] is imperative that we act in a way that does not threaten to fracture the international coalition of nations committed to the dual-track approach, does not inadvertently redound to Iran's economic benefit, and brings real and meaningful pressure to bear on Iran". Circumstances changed after the EU – fearful of an imminent Israeli strike on Iran – displayed willingness to impose an embargo on Iranian crude oil, and Congress provided the president with required waiver authority and the ability to ensure implementation would not rattle the oil markets. In particular, the president can exempt banks for 180-day periods, if he certifies that the parent country had "significantly" reduced its petroleum purchases from Iran over the course of the preceding 180 days. He also can issue a renewable 120-day waiver to exempt countries by invoking U.S. national security interests. Although lifting this sanction would require congressional action, the president enjoys a measure of flexibility, because the legislation does not define what "significant reduction" means. See Section 1245 of National Defense Authorization Act (NDAA) of 2012, Public Law: 112-81, 31 December 2011.
[57] Executive Order 13599, Blocking Property of the Government of Iran and Iranian Financial Institutions, 5 February 2012.
[58] Executive Order 13622, Authorizing Additional Sanctions With Respect to Iran, 30 July 2012. The order essentially sanctions any new customer of Iranian energy products, as NDAA exemptions apply solely to existing ones.
[59] The legislation prohibits the following: any contribution to the enhancement of Iran's ability to develop petroleum resources (both inside and outside the country); assisting Iran in shipping its crude oil or refined petroleum, including by providing underwriting services, insurance or reinsurance for the National Iranian Oil Company (NIOC), the National Iranian Tanker Company (NITC); and purchasing, subscribing to or facilitating issuance of Iranian sovereign debt. It also penalises providers of specialised financial messaging services to blacklisted Iranian banks and bars Iranian students from studying in the fields of energy, nuclear science and nuclear engineering at U.S. universities. Most importantly, section 504 makes repatriating Iran's oil export earnings a sanctionable act, thus forcing Tehran to barter with its remaining oil clients. See Iran Threat Reduction and Syria Human Rights Act of 2012, H.R. 1905 – Public Law: 112-158, 10 August 2010.
[60] Iran Freedom and Counter-Proliferation Act of 2012, Subtitle 1241 of the National Defense Authorization Act of 2013. Repealing or amending NDAA 2013 requires Congressional action, but the

sectors in Iran as "entities of proliferation concern". It also bars the sale, supply and transfer of precious and semi-finished metals to Iran by any person, thereby blocking its ability to be paid in gold for its energy exports and paralysing its manufacturing and housing sectors, which depend on the import of iron and steel; prohibits the provision of insurance or reinsurance to blacklisted entities by any individual or entity; and sanctions the state-owned radio and television agency and its president.[61]

B. *Coordinated Multilateral Sanctions*

To a large degree, the effectiveness of U.S. sanctions depends on coordinated action by other countries. In particular, getting Europe on board was seen in Washington as a critical step. For years, the EU had opposed the U.S. approach, choosing instead to expand its economic ties with Tehran in the late 1990s and early 2000s.

Things changed after 2005, when the joint French, British and German diplomatic endeavour collapsed. Endorsing the first UN Security Council sanction resolution in 2006 as "a necessary and proportionate response to Iran's disregard for the concerns of the international community", the Council of the EU adopted an initial set of sanctions in February 2007.[62] A virtual carbon copy of UN Security Council Resolution (UNSCR) 1737, adopted two months prior, the legislation prohibits provision of nuclear proliferation-related assistance or technology to Iran and imposes travel bans and asset freezes on designated individuals and entities involved in the country's nuclear program.[63] The EU subsequently added an arms embargo and ban on lending.[64] Between 2008 and 2010, it repeatedly amended existing legislation, adding new names and resolving ambiguities.[65]

In 2010, reacting to Iran's continued nuclear activities, decision to enrich at higher levels (20 per cent) as well as apparent snubbing of Obama's offer to engage, Brussels went further. The measures target the Islamic Republic's energy, trade, transporta-

president enjoys various waiver authorities. See Josh Rogin, "White House opposed new Iran sanctions", *Foreign Policy* (online), 30 November 2012. The administration obtained exemptions, notably the right to waive sanctions on Iran's crude oil customers if "exceptional circumstances prevented the country from being able to reduce significantly its purchases of petroleum and petroleum products from Iran".

[61] These measures (with the exception of ban on precious metals trade) do not apply to countries exempted under the National Defense Authorization Act of 2012 and purchases of natural gas. The bill also extended secondary U.S. sanctions to any foreign person doing business with an entity or person on the Treasury Department's Specially Designated Nationals (SDN) list.

[62] Council Conclusions on Iran, 2776th EU External Relations Council meeting, Brussels, 22 January 2007 and Council Common Position 2007/140/CFSP, Concerning restrictive measures against Iran, 27 February 2007. EU sanctions are referred to as "restrictive measures" in Brussels' parlance. This was the first time the EU employed sanctions for non-proliferation-related goals (as opposed to terrorism or human rights). See Aniseh Bassiri Tabrizi and Ruth Hanau Santini, "EU Sanctions against Iran: new wine in old bottles?", Istituto per gli Studi di Politica Internazionale, March 2012. Council Conclusions reflect political agreement between member states on restrictive measure but are not legally binding. They are followed by Council Decisions adopted unanimously and are legally binding, as well as by Council Regulations, which are adopted by a qualified majority (although in practice they tend to be unanimous decisions). Regulations are directly applicable in the EU and are binding for all natural and legal persons in the Union.

[63] Council Common Position 2007/140/CFSP, Concerning restrictive measures against Iran, 27 February 2007.

[64] Council Common Position 2007/246/CFSP, amending Common Position 2007/140/CFSP concerning restrictive measures against Iran, 23 April 2007.

[65] See Appendices A and B below and table on www.crisisgroup.org for lists of amendments.

tion, banking and insurance sectors;[66] restrictions include, inter alia, a ban on investments, sales, supply or transfer of equipment and technology to Iran's energy sector and require member states to inspect suspicious cargo to and from Iran. These were followed in April 2011 by human rights-related sanctions.[67] In the aftermath of the November 2011 IAEA report on the possible military dimension of Iran nuclear activities, the UK and Canada severed all ties with Iran's financial system, including the CBI.[68] The EU also expanded its list of designated entities and began examining options for broadening existing sanctions.[69]

As time elapsed, with diplomacy remaining stalled and prospects of an Israeli military strike seemingly rising, the EU upped its pressure. An EU parliamentarian said, "we need to put more pressure on Iran to quiet the talk of war. The last thing Europe wants amid an economic crisis is another war in the Middle East playing havoc with global oil markets".[70] In January 2012, against this backdrop, Brussels decided to boycott Iranian oil and petrochemical products (effective as of 1 July 2012); ban insurance for their shipments; freeze CBI assets; prevent delivery of the CBI's newly minted banknotes and coinage; block exports of petrochemical equipment and technology; and bar the trade of diamonds and precious metals with Iran.[71]

Among the most damaging steps was the EU's March 2012 decision to prevent Iran's access to financial messaging services for clearing banking transactions.[72] As a

[66] Council Decision 2010/413/CFSP, Concerning restrictive measures against Iran and repealing Common Position 2007/140/CFSP, 26 July 2010. The legislation prohibits the supply of equipment or loans to Iran's oil and gas sector; bans financial transactions with designated persons and entities; mandates notification for transfers of over €10,000 and authorisation for those in excess of €40,000; and bans renewal and extension of insurance or reinsurance contracts executed before the legislation's enactment.

[67] In addition to listing purported human rights violators, the EU Council imposed an embargo on telecommunications monitoring and interception equipment, as well as other technology potentially used for repressive purposes. Council Decision 2011/235/CFSP, Concerning restrictive measures directed against certain persons and entities in view of the situation in Iran, 12 April 2011.

[68] After the decision's announcement, protestors attacked and vandalised the British embassy in Tehran. Despite the Iranian government's expression of regret, London withdrew its embassy staff and expelled Iranian diplomats, reducing diplomatic ties to the lowest level in years. A few months later, Canada severed diplomatic relationship with Iran. See "انتقاد آیت‌الله خامنه‌ای از حمله به سفارت بریتانیا در تهران" ["Ayatollah Khamenei's criticism of the British embassy storming"], BBC Persian, 7 August 2012. Holly Dagers, "Another Embassy Closed in Iran: What Does It Mean for Iranians?", The Huffington Post, 9 November 2012.

[69] Council Conclusions on Iran, 3130th Foreign Affairs Council meeting, Brussels, 1 December 2011.

[70] She continued: "We will pay a devastating price for any strike on Iran, since unlike the U.S., Europe is accessible and can become the target of retribution and terrorism". Crisis Group interview, Brussels, May 2012.

[71] See Council Conclusions on Iran, 3142nd Foreign Affairs Council meeting, Brussels, 23 January 2012 and Council Decision 2012/35/CFSP amending Council Decision 2010/413/CFSP. EU purchases of Iranian oil amounted to nearly 600,000 barrels per day, roughly 18 per cent of Iran's total exports. The EU agreed to a gradual winding down of imports in order to accommodate its most vulnerable members, notably Greece, Spain and Italy, which imported more than 10 per cent of their total consumption from Iran. Tehran initially downplayed the embargo's impact and threatened to pre-emptively halt oil exports to Europe. Eventually, in a largely symbolic move, it stopped sending oil to France and the UK, which respectively imported only about 1 and 4 per cent of their total oil consumption from Iran. Oil prices momentarily rose to an eight-month high (see Joby Warrick, "Iran halts oil shipments to Britain, France", *The Washington Post*, 29 February 2012), but increased production from Libya, Iraq and Saudi Arabia cancelled out the embargo's impact on the EU and oil prices.

[72] Council Regulation 267/2012, Concerning restrictive measures against Iran, 23 March 2012.

result, the Belgium-based Society for Worldwide International Financial Transfers (SWIFT), considered the world's primary financial clearing house, cut off all EU-designated Iranian banks from its network, thereby essentially preventing any foreign transactions with them.[73] After several unsuccessful rounds of meetings between the P5+1 and Iran, the EU again ratcheted up sanctions, banning among other things transactions between European and Iranian banks (unless specifically authorised and except for those related to food and medicine supply) and imports of Iranian gas, as well as exports of graphite, semi-finished metals (such as aluminium and steel) and ship-building equipment or technology to Iran.[74]

Several other countries, such as Japan, South Korea, Australia, New Zealand, Canada, Switzerland and Norway, joined in the sanctions, closely aligning themselves with U.S. or EU decisions.

C. *United Nations Sanctions*

In February 2006, faced with Iran's refusal to suspend its enrichment program, the IAEA referred the case to the Security Council, which over time adopted a series of resolutions sanctioning Tehran for non-compliance.[75] UNSCR 1696 requested Iran to take the IAEA-mandated steps and suspend its uranium enrichment activities within 30 days;[76] in light of Iran's failure to cooperate, the Council adopted Resolution 1737, which barred supply of nuclear-related materials and technology and imposed a travel ban as well as asset freeze on individuals and entities related to Iran's nuclear and ballistic missile programs.[77] The resolution called upon states to prevent Iranian students from studying in sensitive branches liable to contribute to the na-

[73] Lázaro Campos, CEO of SWIFT, stated: "Disconnecting banks is an extraordinary and unprecedented step for SWIFT. … This EU decision forces SWIFT to take action", quoted in "SWIFT instructed to disconnect sanctioned Iranian banks following EU Council decision", SWIFT press release, 15 March 2012.

[74] The EU insists that these sanctions do not amount to a total trade ban. Transactions involving foodstuffs, healthcare, medical equipment or items related to agricultural and humanitarian purposes in amounts under €100,000, as well as personal remittances amounting to less than €40,000, do not require prior authorisation. See Council Decision 2012/635/CFSP, Concerning restrictive measures against Iran, 15 October 2012.

[75] In retaliation, Iran halted its voluntary implementation of the IAEA's Additional Protocol. Implementation of the NPT Safeguards Agreement in the Islamic Republic of Iran, GOV/2006/15, IAEA, 27 February 2006. According to Iran's ambassador to the IAEA, Ali Ashghar Soltanieh, the Security Council resolutions have no legal basis for at least five reasons: Iran's suspension of enrichment was a voluntary measure and non-legally binding, thus resumption of enrichment could not be the basis for a referral; Article XII.C of the IAEA's statute only applies to diversion of nuclear material provided by the agency, not to indigenously produced material as in the case of Iran; there is no proof of diversion of nuclear material for military purposes; UN inspectors monitoring Iran's declared facilities have faced no obstacles; and IAEA inspectors have yet to report an instance of Iranian noncompliance. Crisis Group interview, Vienna, 16 May 2012. For a thorough review of this issue, see Paul Kerr, "Iran's Nuclear Program: Tehran's Compliance with International Obligations", Congressional Research Service, 18 September 2012.

[76] UN Security Council Resolution 1696, 31 July 2006.

[77] According to the resolution, UN sanctions will be suspended if and for as long as Iran suspends all enrichment-related and reprocessing activities, including research and development, as verified by the IAEA, to allow for negotiations. The measures will be terminated when the IAEA determines that Iran has fully complied with its obligations under relevant UNSC resolutions and met the IAEA Board's requirements. The resolution exempts supply of equipment for light water reactor as well as nuclear fuel to Iran. See UN Security Council Resolution 1737, 27 December 2006.

tion's nuclear and missile programs. Three months later, UNSCR 1747 expanded the list of designations, banned loans and financial assistance to Iran except for developmental and humanitarian purposes, prohibited Iranian arms exports and imposed a conventional weapons arms embargo.[78]

It took another year for Security Council permanent members to agree on a further round of sanctions. In March 2008, UNSCR 1803 expanded the list of designated Iranian firms and individuals, required member states to inspect Iranian cargos if there were "reasonable grounds" to believe they contained prohibited goods[79] and called upon all countries to show vigilance in financial dealings with Iranian banks.[80]

After difficult negotiations among Security Council permanent members, and against the backdrop of the disclosure of a concealed nuclear facility in Fordow coupled with the announcement of Tehran's 20 per cent enrichment, the Council adopted UNSCR 1929.[81] It proscribes the sale of conventional heavy weapons to Iran, expands the list of designated entities and individuals and makes previous travel bans binding, authorises countries to inspect any Iranian shipment, bars Iranian investment in other countries' uranium mining and related activities, bans the provision of financial services (including insurance or re-insurance) to Iranian entities suspected of involvement in the nuclear program and prohibits Iranian banks from opening new foreign branches. The Council has been unable to reach agreement on additional sanctions since June 2010, mainly due to opposition by Russia and China.

D. *Shell Games: Enforcement and Evasion*

Effectiveness of the sanctions regime hinges on enforcement, a cat-and-mouse game between Iranian efforts at circumvention and attempts by others to plug loopholes.[82] The U.S. took the lead in this regard, penalising foreign banks and firms that violated its regulations.[83] Too, there was a chilling effect: with several high-profile cases in-

[78] UN Security Council Resolution 1747, 24 March 2007. Then-Iranian Foreign Minister Manouchehr Mottaki reacted with the following statement to the Council, 24 March 2007: "If you are seeking to sanction and block the wealth and capabilities of the Iranian nation, particularly our national heroes [scientist and revolutionary guards], who are mentioned in the resolution, then I will tell you what [our] main assets are: faith in God, seeking justice, and resisting against threats and intimidations. Can this resolution block these valuable assets?"
[79] Subsequent resolutions specified that inspections of vessels in international waters, in contrast to national waters, require consent of the vessel's flag state.
[80] UN Security Council Resolution 1803, 3 March 2008.
[81] UN Security Council Resolution 1929, 9 June 2010. This was the first non-unanimous resolution sanctioning Iran. Turkey and Brazil, both members at the time, voted "no" to signal their displeasure after the U.S. and others rejected the nuclear swap deal they had brokered with Iran; Lebanon abstained. Resolution 1929 added two new demands to previous requirements, notably that Iran ratify the Comprehensive Nuclear-Test-Ban Treaty and stop developing ballistic missiles capable of carrying nuclear weapons.
[82] For an overview of how various countries coordinate their efforts to comply with UN sanctions, see "Final report of the Panel of Experts established pursuant to resolution 1929", UN, 2012, according to which the percentage of member states submitting a report on implementation of UNSCR 1929 increased from 25 per cent in 2011 to 40 per cent in 2012.
[83] May 2011 saw the first sanctions against companies (registered in Venezuela, the UAE, Jersey, Singapore, Monaco and Israel) due to involvement in petrol trade with Iran, a violation of ISA regulations (as amended by CISADA). "Seven Companies Sanctioned Under the Amended Iran Sanctions Act", U.S. State Department, 24 May 2011. In July 2012, The Obama administration also imposed the first penalties on violators of CISADA's banking provisions, blacklisting an Iraqi and a

volving penalties against major international financial institutions (eg, Lloyds, Barclays, Credit Suisse and Standard Charter), other companies became more prudent;[84] in some cases, firms took extra precautions that affected permissible trade.[85] Many small and mid-sized companies, for whom compliance with overlapping and layered regulations was too costly and cumbersome, simply left the Iranian market.[86] Several Persian Gulf countries, traditionally averse to alienating their powerful neighbour, more dutifully respected sanctions.[87] Even when it still enjoyed relatively close ties to Iran, Turkey occasionally inspected Iranian air and land cargo, impounded arms shipments supposedly en route to Syria and Lebanon and reported these incidents to UN officials.[88]

Even so, the sanctions regime remains far from ironclad, and Iran has proved adept at both evasion and covering its tracks. A senior Iranian official said, "after living under sanctions for three decades, we are now in a position to open up a consultancy and share our know-how with other countries facing a similar situation!".[89] A Dubai-based Iranian businessman explained, "before sanctions enforcement was ramped up, conducting business with Iran was high value and low risk. Now, it is high value and high risk. But there still are many companies willing to take calculated risks".[90] Several small financial institutions in Asia, with no relation to U.S. or European counterparts, make large profits by facilitating transactions for Iranian clients.[91] Front companies procure banned goods, launder funds and transport products to Iran through neighbouring countries, often operating via numerous interme-

Chinese bank. "Treasury Sanctions Kunlun Bank in China and Elaf Bank in Iraq for Business with Designated Iranian Banks", U.S. Treasury Department, 31 July 2012.

[84] U.S. regulators levied a $100 million fine against Switzerland's UBS bank in 2004; $80 million against Dutch bank ABN Amro in 2005; $350 million against Britain's Lloyds TSB and $536 million against Switzerland's Credit Suisse in 2009; $298 million against Britain's Barclays in 2010; as well as $619 million against Dutch bank IMG, $8.6 million against Japan's Bank of Tokyo-Mitsubishi UFJ and $674 million and $1.92 billion respectively against Britain's Standard Chartered Bank and HSBC, in 2012 for unauthorised transactions with Iran and other sanctioned countries. See Katzman, "Iran Sanctions", op. cit.

[85] Crisis Group interview, UN Panel of Experts member, New York, 24 July 2012.

[86] A European businessman said, "the problem is that the regulations change all the time. So even if your dealings with Iran are authorised at the time of signing the contract, there is no guarantee that this will remain true at the time of delivering the products". Others expressed similar concerns. Crisis Group interviews, European and Iranian businessmen, Brussels, Istanbul, Dubai, April-December 2012.

[87] Louis Charbonneau, "Bahrain, UAE probe suspicious shipments headed to Iran", Reuters, 18 September 2012. A Dubai-based Iranian trader said, "I can no longer pay my office rent in Dubai using my account at the local branch of an Iranian bank. This transaction has nothing to do with Iran, but the Emiratis have blocked it". Others described their situation as "encircled by sanctions" and complained of zealous enforcement of U.S. and international restrictive measures by Emirate officials. Crisis Group interview, Dubai, April 2012.

[88] See "Final report of the Panel of Experts", op. cit.

[89] Crisis Group interview, September 2012. Other officials have stressed the nation's ability to bypass the sanctions. See "رهبر انقلاب: تحریمها را دور میزنیم" ["Leader of the Revolution: We will skirt sanctions"], Tabnak.ir, 8 September 2010; "احمدینژاد: تحریمها را دور میزنیم" ["Ahmadinejad: We will skirt Sanctions"], BBC Persian, 4 December 2012.

[90] Crisis Group interview, Dubai, April 2012. Also see "Small Russian banks help Iran's oil exports: minister", Reuters, 12 February 2013.

[91] Crisis Group interviews, Iranian businessmen, Istanbul, August 2012.

diaries.[92] Tellingly Iranian markets are awash in U.S. consumer goods, ranging from Apple products to popular clothing brands, often reshipped from Asian countries via Dubai.[93]

Iran has sought to parry sanctions in other ways. For a while, it countered the blacklisting of major shipping companies by renaming and reflagging its vessels, registering them in poorly-regulated jurisdictions[94] or disabling their tracking devices to conceal their movements.[95] When, under U.S. pressure, numerous countries began shutting their doors to Iranian shipping companies,[96] Tehran resorted to other tactics. It blended its oil with products from other countries,[97] boosted production and exports of less scrutinised petroleum products such as fuel oil,[98] used remote storage facilities to conceal large oil shipments and avoided port authorities by conducting mid-ocean ship-to-ship transfers.[99] The affair took on the appearance of a never-ending game of whack-a-mole[100] that the U.S. has sought to render moot by targeting entire sectors of Iran's economy.[101] But for many ordinary citizens, skirting sanctions has become a way of life. An Iranian trader explained:

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[92] Some of these schemes are highly complex, increasing their effectiveness but also their cost. Crisis Group interviews, Iranian businessmen and financiers, Dubai, Istanbul, April, August 2012. For an overview of sixteen sanction-busting techniques frequently employed by Iran, see Mark Dubowitz, "So You Want to Be a Sanctions-Buster", *Foreign Policy* (online), 10 August 2012.

[93] Iranian sailors at Dubai Creek complained about the lacklustre business environment in their home country, reduced purchasing power and financial restrictions, yet they continued to shuttle between Iranian ports and Dubai, transporting various types of consumer goods. Crisis Group interviews, Dubai, April 2012; see also Karim Sadjadpour, "The Battle of Dubai: the United Arab Emirates and the U.S.-Iran Cold War", Carnegie Endowment for International Peace, July 2011. After Malaysia and the UAE began cracking down on shell companies smuggling sensitive technologies to Iran, China, Taiwan and Singapore reportedly stepped in to fill part of the vacuum. See Ken Dilanian, "Illegal exports to Iran on the rise, say U.S. officials", *Los Angeles Times*, 17 November 2012; Shashank Bengali, "One shady operator provides glimpse of supply line to Iran", *Los Angeles Times*, 21 October 2012; Nasser Karimi and Brian Murphy, "Iran Sanctions: American brands still find their way to Iran", Associated Press, 14 September 2012.

[94] Although each ship possesses a unique identification number assigned to it by the International Maritime Organization, some port authorities looked the other way if the vessel had no visible connection to Iran. Crisis Group interview, UN official, New York, July 2012. Between September 2008 and February 2012, the Islamic Republic of Iran Shipping Lines (IRISL) and its related companies changed the name, flag or ownership details of the 144 vessels in their fleet at least 878 times. See Rachel Armstrong, Stephen Grey and Himanshu Ojha, "Iran's global cat-and-mouse game on sanctions", Reuters, 15 February 2012.

[95] Christopher Johnson and Peg Mackey, "Iran ships 'off radar' as Tehran conceals oil sales", Reuters, 13 April 2012.

[96] Richard Valdmanis, "Tuvalu to stop reflagging Iranian ships following US pressure", and "Sierra Leone removes nine Iranian vessels from shipping register", Reuters, 8 September 2012; Benoit Faucon and Colum Murphy, "Iran Shippers Face Difficulty Dodging Sanctions", *The Wall Street Journal*, 28 September 2012.

[97] Crisis Group telephone interviews, Iranian oil experts, Tehran, September 2012.

[98] Humeyra Pamuk and Emma Farge, "Iran sidesteps sanctions to export its fuel oil", Reuters, 20 December 2012.

[99] Luke Pachymuthu and Randy Fabi, "Iran parks oil off Malaysia to dodge Western sanctions", and "Vitol trades Iranian fuel oil, skirting sanctions", Reuters, 13 and 26 September 2012.

[100] Crisis Group interview, U.S. officials, Washington, December 2012.

[101] The National Defense Authorization Act of 2013, which targets large swathes of the Iranian economy, is a step toward a total trade embargo. See Joby Warrick, "New Iran sanctions target industry in bid for deal curbing nuclear program", *The Washington Post*, 6 January 2013.

> The reason I go through several middlemen and front companies is not that it is profitable. I have neither nefarious intentions nor ties with the government or IRGC (Islamic Revolutionary Guards Corps). I do it because I need to make ends meet. So if sanctions close the door, I have to come in from the window; and if they close the window, I have no choice but to use the chimney.[102]

The patchwork of sanctions now imposed on Iran is impressive. It has effectively impaired its main source of income, the export of oil and petroleum products; cut off its banking infrastructure from the global financial system; forced it to engage in inefficient barter deals; and stymied imports of dual-use goods, but also indirectly in some cases basic food staples and medicines.[103] Unilateral and multilateral restrictive measures, with multiple triggers and targets, are more sweeping than their UN counterparts and have hurt Iran the most.

In the face of their apparent ineffectiveness at producing the desired changes in Iranian policies, however, some policymakers and analysts have called for a further tightening of the screws, arguing that the regime barely has felt their impact and that only the prospect of genuine economic collapse – of a type that theoretically would threaten the Islamic Republic's survival – can succeed. Among possible candidates for more sweeping sanctions are: a total trade and investment embargo (exempting food and medical products); an international ban on Iran's energy exports; interdiction of all passenger and cargo flights to and from Iran; a ban on its officials from travelling; and expulsion of the country from international organisations.[104] Although it is impossible to disprove the argument, it is at least highly questionable whether even such onerous measures can persuade a leadership seemingly convinced that the only thing more dangerous than this threat would be to surrender to it.[105]

[102] Crisis Group interview, Istanbul, August 2012.
[103] Financial restrictions and transportation obstacles purportedly temporarily impeded Iran's imports of wheat, rice, chicken feed and cooking oil in 2012. See Niluksi Koswanage and Parisa Hafezi, "Signs build that Iran sanctions disrupt food imports", Reuters, 8 February 2012; Glenn Greenwald, "Iran sanctions now causing food insecurity, mass suffering", *The Guardian*, 7 October 2012.
[104] Crisis Group interviews, U.S. analysts, Washington, February 2013.
[105] A member of Iran's negotiating team wrote: "In reality, Iran has surmounted the highest peak of sanctions and has been able to adapt its vital systems to it. Perhaps the Americans will be able from now on to change the price of a certain commodity for a limited period of time, but Iran will leave no place for ambiguity over the fact that its centrifuges are still spinning and will be never dismantled". See Mohammadi, "بن بست یا گشایش؟، 2013", op. cit.

III. The Impact of Sanctions

The effects of sanctions are as complex as the nature of the sanctions regime itself. Not all actors and sectors have felt the consequences equally or precisely as intended. Circumstances have been in constant flux as sanctions evolve and expand and as Tehran learns to adapt and adjust. Difficulties in disaggregating the consequences of sanctions from the self-inflicted wounds of Iranian mismanagement and structural problems, coupled with information scarcity, make any reliable assessment challenging. Finally, one must bear in mind different objectives and thus different measures of success: to the extent some sanctions were designed to affect Iran's human rights practices, the record is rather bleak.[106] Nor, for example, has there been any notable success in curbing Tehran's support for state and non-state allies.[107] In other areas – the nuclear program in particular – the assessment arguably is more mixed.

A. *Impact on the Nuclear and Missile Programs*

Over the past three decades, Tehran has made significant progress in acquiring nuclear and missile domestic capability and know-how. Still, it continues to depend on outside suppliers for procurement of key material and critical components.[108] Thus, although most components in its gas centrifuges are built indigenously, sanctions almost certainly have contributed to slowing down the pace of production, notably at its main facility in Natanz.[109] Enhanced export controls likewise have impeded Iran's acquisition of dual-use material and equipment, such as maraging steel, carbon fibre, vacuum pumps and measuring equipment. A similar predicament has retarded ef-

[106] There has been no palpable change in the number of executions, political detentions and imprisoned journalists. Crisis Group interviews, Iranian human rights activists, Washington, Brussels, April-December 2012. See also "Freedom in the World", Freedom House, 2006-12.
[107] Iran's support for the Syrian regime appears to have been steady – and even increasing – since the uprising began. Crisis Group interviews, U.S., French officials, Washington, Paris, January-February 2013. See "Tehran denies Revolutionary Guards in Syria", Agence France-Presse, 17 September 2012; Michael Peel and Najmeh Bozorgmehr, "Iran gives Syria $1 bn import credit line", *Financial Times*, 16 January 2013. In February, Iran acknowledged the loss of a Revolutionary Guards general in Syria. See Farnaz Fassihi, "Iranian general is killed in Syria", *The Wall Street Journal*, 13 February 2013. Iran boasted that it had provided Hamas rocket technology that it used during the November 2012 conflict with Israel. Ali Larijani, the speaker of the Iranian parliament, said, "we proudly say we support the Palestinians, militarily and financially. The Zionist regime needs to realise that Palestinian military power comes from Iranian military power …. We may have inflation, unemployment and other economic issues in our country, but we are changing the region, and this will be a big achievement". Quoted in Thomas Erdbrink, "Iranian missiles in Gaza fight give Tehran government a lift", *The New York Times*, 21 November 2012. For more on the Gaza war, see Crisis Group Middle East Report N°133, *Israel and Hamas: Fire and Ceasefire in a New Middle East*, 22 November 2012.
[108] Crisis Group interview, Olli Heinonen, former IAEA deputy director general, Washington, 7 February 2013.
[109] Not all these setbacks are the result of procurement problems; some appear to have been caused by sabotage and cyber-attacks. See David Albright, Paul Brannan, Andrea Stricker, Christina Walrond, and Houston Wood, "Preventing Iran from Getting Nuclear Weapons: Constraining its Future Nuclear Options", Institute for Science and International Security, 5 March 2012. Iran's stated objective was to install 50,000 centrifuges in Natanz by 2011. According to the IAEA, as of February 2013 only roughly 25 per cent of the facility was operational. See Report by director general, IAEA, GOV/2013/6, op. cit. Jay Solomon and Charles Levinson, "Sanctions slow Iran's warhead capability", *The Wall Street Journal*, 8 January 2011.

forts to mass-produce advanced centrifuges rather than the outdated IR-1 machines, while delaying construction of its heavy-water reactor in Arak.[110]

The impact of sanctions equally can be felt in the realm of medium- and long-range ballistic missile production. Solid fuel systems in particular require foreign materials, such as aluminium and tungsten powder as well as oxidiser salts, disruption in the supply of which compels use of sub-standard substitutes.[111] The lengthy delay in test-flying the two-stage 2,000km range solid-fuelled Sajjil-2 missile, on hold since February 2011, arguably is an illustration.[112] These challenges appear to have had the most significant effect on development of longer-range missiles, possibly bringing intercontinental ballistic missiles efforts to a temporary halt.[113]

Despite such substantial setbacks, both the nuclear and missile programs have grown, and so too in parallel have Western concerns.[114] Since international and multilateral sanctions aimed at curbing Iran's nuclear activities were imposed in 2006, advances have occurred on several fronts: the nuclear facility in Fordow became operational; Iran has enriched uranium to 20 per cent level; and the Bushehr nuclear reactor was completed.[115] Moreover, Tehran persists in conducting regular missile tests, unveiling new generations of short- and medium-range missiles, improving their accuracy and refurbishing missiles to send satellites into space.[116]

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[110] Iran's IR-1 centrifuges are based on a four-decade old Dutch design, obtained from the Pakistani black marketer Abdul Qadeer Khan. They are inefficient and prone to regular mechanical failures. See Simon Henderson and Olli Heinonen, "Nuclear Iran: Technical Issues Overshadowing Negotiations", Washington Institute of Near East Policy, 23 October 2012. The new generation of more sophisticated centrifuges (IR-2m, IR-4, IR-5, IR-6, and IR-6s) is believed to be three to four times more efficient. Crisis Group interview, nonproliferation expert, Vienna, December 2012. Iran has been testing these machines during the past few years and as of February 2013 had deployed three cascades of various sizes of IR-2m and one cascade of IR-4 machines at the Natanz nuclear facility. See "Implementation of the NPT Safeguards Agreement and relevant provisions of Security Council resolutions in the Islamic Republic of Iran", Report by director general, IAEA, GOV/2013/6, 21 February 2013. The IAEA also reported that Iran had postponed the completion date of Arak's heavy-water reactor from 2013 to 2014, most likely due to export-control related setbacks. See Kelsey Davenport, Daryl G. Kimball, and Greg Thielmann, "The November 2012 IAEA Report on Iran and its Implications", Arms Control Now, 16 November 2012.

[111] Crisis Group interview, Greg Thielmann, Arms Control Association, Washington, 5 December 2012.

[112] "Iran sanctions halt long-range ballistic-missile development", The International Institute for Strategic Studies, July 2012.

[113] A new study casts doubt on previous assessments by U.S. intelligence agencies that Iran was on track to test-fly intercontinental ballistic missiles by 2015. See Steven A. Hildreth, "Iran's Ballistic Missile and Space Launch Programs", Congressional Research Service, 6 December 2012.

[114] According to Iran's foreign minister, Ali Akbar Salehi, sanctions "will slow down our work, but they will not bring it to a halt". Crisis Group interview, New York, 25 September 2012. Yukiya Amano, IAEA director general, recently noted: "We have observed that the progression of enrichment has been constant. There has been a steady, gradual increase in the amount [of enriched uranium]". Quoted in "Iran nuclear work at constant pace despite sanctions – IAEA", Reuters, 20 November 2012.

[115] Crisis Group interview, Ambassador Soltanieh, Vienna, 16 May 2012.

[116] In 2012, Iran test-fired its new Fateh-110 missile, with a range of around 300km and thereby capable of reaching all its Persian Gulf neighbours. Modified ballistic missiles were used to launch Iran's Safir and Navid satellites into orbit, in 2011 and 2012 respectively. See Yeganeh Torbati, "Iran unveils new missile, starts air defense site", Reuters, 21 August 2012; "Final report of the Panel of Experts", op. cit.; "Annual Report of Military Power of Iran", U.S. Department of Defense, April 2012. Notwithstanding such advances, Iran's conventional deterrence has deteriorated signif-

B. *Impact on the Energy Sector*

Iran's combined oil and natural gas reserves – the world's largest hydrocarbon supply – is by far the principal source of its government's revenues and thus the most obvious target of sanctions.[117] Over the years, the U.S. – subsequently joined by the EU – developed a three-pronged strategy to choke off this income stream. The first, reflected in the 1996 Iran Sanctions Act, was to proscribe investments in the country's oil and gas infrastructure, thereby stunting growth and hampering maintenance. Enforcement was uneven, largely because Washington sought to accommodate its allies' commercial interests in Iran. Yet, the chilling effect – combined with Iran's unattractive contract terms – discouraged investors.[118]

Consequences have been far-reaching. Iran's aged oil fields witnessed steep declines in production rates,[119] and stemming or reversing these trends reportedly would require at least $300 billion of investment over the next decade.[120] At the same time, major firms have withdrawn or wound down their ties, meaning a net loss of potential investments in its energy sector estimated at roughly $60 billion.[121] Nor has the withdrawal of Western firms been truly compensated by Asian and Eastern European companies, which also have largely shunned Iran's energy sector.[122] As an

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icantly due to years of international isolation and an arms embargo. At the same time, regional neighbours have acquired billions of dollars of sophisticated weaponry.

117 "Country Analysis, Brief for Iran", U.S. Energy Information Administration. In 2011, oil revenues constituted about 72 per cent of its foreign currency earnings. See See Akbar Torkan and Hamed Farnam, "مدیریت منابع نفتی و تامین مالی پروژه هاي نفتی" ["The Management of Oil Resources and Funding Oil Projects"], Centre for Strategic Research – The Expediency Council and the Islamic Republic of Iran, October 2012, at www.csr.ir/Pdf/Content2589/156.pdf.

118 An Iranian energy expert said, "Iran had many chances in the past to sign contracts with major oil and gas companies. But it failed to do so when companies like Total, ENI and others were lining up. Had the contracts been signed, and major Western companies had financial stakes in the country, the game certainly would have been very different. Instead, the Iranians over-negotiated and demanded a contract framework that did not match the companies' risk-return analysis. Had Iran better identified its key strategic interests, it would have agreed to slightly higher remuneration rates for big international oil companies, and they in turn might have lobbied against severe sanctions". Crisis Group interview, Siamak Namazi, Dubai, 12 December 2012. Many oil industry experts believe that the Iranians have been their own worst enemies in this regard. Iran was ranked 145 out of 185 countries on the 2011 World Bank index of ease of doing business. See http://data.worldbank.org/indicator/IC.BUS.EASE.XQ.

119 The decline, caused by reservoir damage, reduced gas pressure and decrease in existing deposits, is estimated to be as high as 8 per cent for onshore and 10 per cent for offshore fields. This represents an annual crude oil production loss of somewhere between 400,000 and 500,000 barrels per day. See U.S. Energy Information Agency, op. cit. Some Iranian lawmakers have warned that at these rates and given growing domestic consumption, the country could become a net oil importer this decade. See "کمیسیون انرژی مجلس: هفت سال دیگر صادرات نفت ایران قطع می شود" ["Parliament's Energy Commission: Iran's oil exports will end in seven years"], *Siyasat Rouz*, 14 April 2011.

120 "وزیر نفت خبر داد. نیاز ۰۰۳ میلیارد دلاری صنعت نفت به سرمایه گذاری" ["Iran's Minster of Oil: The oil industry needs $300 billion in investment"], *Siyasat Rouz*, 8 November 2011. Although oil experts diverge on the amount of foreign capital required to reinvigorate the country's hydrocarbon industry, no one disputes the need for investment capital and modern technology. Crisis Group interviews, Washington, Istanbul, August 2012.

121 See Jackson Flavia Krause, "Sanctions cost Iran $60 billion in oil investments, Burns says", Bloomberg, 1 December 2010. Of the 42 foreign firms engaged in Iran's energy sector in 2005, 27 withdrew by September 2012. For a complete list, see "Firms Reported to Have Sold Iran Refined Petroleum Products or Engaged in Commercial Activities in Iran's Energy Sector", GAO-13-173R, U.S. Government Accountability Office, 7 December 2012.

122 Crisis Group interviews, oil experts, Dubai, Brussels, April, October 2012.

imperfect fall-back, Iran has had to turn to domestic investors, notably its own Revolutionary Guards. A former Iranian official asked: "Should we abandon our development projects just because European and American companies have turned their backs on us? Who other than the IRGC, with years of experience in constructing tunnels and bridges, could take over?"[123]

Overall, the International Energy Agency (IEA) predicts that even if the nuclear crisis were to be resolved promptly and sanctions lifted, Iran would not be in a position to recover its production rate of nearly four million barrels a day (b/d) before 2020.[124] Sanctions also have stymied Iran's efforts to cultivate its vast natural gas potential. Despite holding the world's second largest natural gas reserves, it ranks only 25th on the list of natural gas exporters.[125]

This reality notwithstanding, Iran still generated record oil and gas revenues due to high prices, leading the U.S. to rely on a second strategy.[126] The goal was to target oil payment mechanisms, specifically countries that used Iran's central bank to process revenues.[127] Both sides initially doubted the effectiveness of this policy, but compliance was facilitated by an oil market saturated with additional supply.[128] As a result, all major Iranian oil importers either halted or reduced their purchases.[129]

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[123] Crisis Group telephone interview, Tehran, August 2012. The IRGC reportedly benefited most from lucrative projects that had been abandoned mid-course. This is true in particular of the construction and engineering conglomerate known as Khatem ol-Anbiya (The Seal of the Prophets). According to Iranian officials, as of July 2011 the IRGC had signed contracts valued at $25 billion in the oil and gas sectors. "است شرکت ملی نفت: قراردادهای نفتی خاتم الانبیاء ۵۲ میلیارد دلار" ["National Oil Company: Khatam ol-Anbiya's Oil Contracts are Worth $25 Billion"], BBC Persian, 31 July 2011. The IRGC also expanded its economic involvement in other key sectors, including telecommunications, construction, banking and transportation. See Frederic Wehrey et al., "The Rise of the Pasdaran", Rand Corporation, 2009; Kaveh Omidvar, "سپاه پاسداران اموال دولتی را تصاحب می‌کند؟" ["The Revolutionary Guards Appropriates State Assets?"], BBC Persian, 28 May 2012. Iranian energy experts offer a more nuanced view. "The IRGC subcontracts its projects to hundreds of Iranian firms, which possess the expertise but do not necessarily share the IRGC's ideological and political beliefs". Crisis Group telephone interview, Iranian energy expert, Tehran, July 2012.

[124] See "World Energy Outlook 2012", Organisation for Economic Cooperation and Development – International Energy Agency, 2012.

[125] With more than two thirds of its natural gas reserves still untapped, Iran's gas exports account for less than 1 per cent of global trade. U.S. Energy Information Agency, op. cit.

[126] During president Ahmadinejad's first seven years in office (2005-2011), Iran generated some $531 billion in oil revenues, dwarfing the $157 billion reached under President Mohammad Khatami (1997-2005) and $141 billion under his predecessor Ali-Akbar Hashemi Rafsanjani (1989-1997). See Torkan and Farnam, "مدیریت منابع نفتی و تامین مالی پروژه هاي نفتی", op. cit.

[127] See Section 1245 of National Defense Authorization Act of 2012.

[128] An Iranian energy expert said, "Iran's perception was that oil sanctions were bound to fail. The Europeans, embroiled in a financial crisis, were not going to shoot themselves in the foot by endangering their energy security; the U.S. was not inclined to risk high oil prices in an election year; and with the region in turmoil, no one was prepared to take OPEC's second largest oil producer by the horns. The assessment was truly Pollyanna-ish". Crisis Group telephone interview, Tehran, September 2012. Another expert said, "underestimating the oil sanctions was a grave mistake. This was not the first time countries gave in to pressure from Washington. In 1995, Japan cancelled its $450 million loan to Iran. The same year, China retracted from a previous agreement to build two 300 megawatt nuclear reactors in Iran". Crisis Group telephone interview, Iranian energy expert, Tehran, August 2012. U.S. officials, too, were uncertain. A senior official said, "it was always a roll of the dice because we didn't know what the reaction was going to be". Quoted in Arshad Mohammed, Justyna Pawlak and Warren Strobel, "Inside the West's economic war with Iran", Reuters, 28 December 2012. To ensure success, U.S. officials worked hard to garner international support and even visited regional oil infrastructure to ensure that increased production could compensate for

The third approach took aim at Iran's ability to transport its oil. The EU barred the provision of insurance for Iranian oil shipments, blacklisted the country's transportation and shipping sectors and sanctioned its ship-building industry.[130] The U.S. followed suit.[131] Consequences of the insurance ban were far-reaching, making shipments of Iranian oil highly risky.[132] Key consumers, including South Korea and Japan, were forced to further reduce their imports.[133] Largely in response, Iran's oil exports dropped from an average of 2.5 million b/d in 2011 to under 1 million b/d in January 2013.[134]

Whereas Iran was able to anticipate and deal with restrictions on the importation of refined petroleum products,[135] it proved far less successful in coping with oil sanctions.[136] After long denying their impact, officials ultimately acknowledged they had

the loss of Iranian crude oil. The swift return of Libya's 1.6 million b/d after Qadhafi's ouster, Iraq's increased production of 650,000 b/d and, most importantly, Saudi Arabia's additional 1.5 million b/d (reaching the historic record of 10 million b/d) helped make up for the loss of Iranian oil. See "World Energy Outlook 2012", IEA, 2012.

[129] Jay Solomon and Keith Johnson, "U.S. renews exemptions from Iran sanctions", *The Wall Street Journal*, 7 December 2012; Trevor Houser, "Iran Sanctions: The Year in Review", Rhodium Group (rhg.com), 11 February 2013.

[130] See Council Decision 2012/35/CFSP, amending Council Decision 2010/413/CFSP, Council Regulation (EU) no. 56/2012 amending Council Regulation (EU) no. 961/2010, Council Implementing Regulation (EU) 54/2012 implementing Regulation (EU) no. 961/2010, Council Regulation (EU) 267/2012.

[131] See Iran Threat Reduction and Syria Human Rights Act and Iran Freedom and Counter-proliferation Act.

[132] "How Iran's main oil buyers deal with insurance sanctions", Reuters, 30 August 2012.

[133] See Katzman, "Iran Sanctions", op. cit.

[134] Anthony DiPaola and Isaac Arnsdorf, "Iran loses $133 million a day on embargo as oil buoys Obama", SFGate/Bloomberg News, 2 August 2012. Export levels rebounded from 850,000 b/d in September 2012 to nearly 1.56 million b/d by the end of the year, as some countries – notably China and South Korea – shifted the insurance burden to Iranian oil tankers, and others, such as Japan and India, established their own sovereign guarantees. See "IEA sees Iran oil sales falling as sanctions bite", Reuters, 13 February 2013. Some oil experts believe that the reduction in Iranian exports is less than believed due to "invisible" sales occurring through mid-ocean swaps and other concealed methods. Crisis Group telephone interviews, Iranian oil experts, Tehran, July 2012. Alternative steps Iran possibly has taken to cope with diminished exports include reducing production across different oil fields (instead of shutting them down at the expense of future productivity recovery); converting some power plants from gas to oil operation; and expanding storage facilities. Offering large discounts to oil customers apparently was deemed unwise as Iranians feared being caught in a downward spiral. Crisis Group telephone interviews, Iranian oil experts, Kharg, October 2012; see also John van Schaik, "Market Forces: Iran is Selling More Than Meets the Eye", Energy Compass, 7 September 2012.

[135] As of 2010, Iran imported nearly 40 per cent of its domestic petrol consumption. With U.S. sanctions looming large, Tehran rationed consumption, scrapped petrol subsidies and boosted its domestic refinery capacity. "Iran is ready for planned U.S. sanctions targeting fuel imports, analysts say", *The Washington Post*, 24 June 2010. However, indigenously-produced petrol is costlier and substandard, exacerbating air-pollution. See Najmeh Bozorgmehr, "Sanctions hit Iran petrol imports", *Financial Times*, 11 October 2012; Mohsen Asghari, "Iran pollution worsens as thousands die", BBC, 7 January 2013. By investing in its own capacity to refine petroleum products, Iran could offset some of the effects of sanctions, given both high regional demand for such goods and greater difficulty in impeding transportation, as well as sale in a market less transparent than its global oil counterpart. Crisis Group telephone interview, Bijan Khajehpour, executive director, Atieh International, Vienna, 7 January 2013.

[136] Production levels have fallen behind regional competitors, such as Iraq, Kuwait and the UAE. See "World Energy Outlook 2012", International Energy Agency – Organisation for Economic Co-

caused "a 40 per cent decrease in oil sales and a 45 per cent decrease in repatriating oil money".[137]

C. *Economic Impact*

Disaggregating the effects of past conflicts, mismanagement, structural deficiencies, and prior and more recent sanctions is no easy task. Each disruption has prompted inflation, currency devaluation, capital flights and brain drain. Analysis is further complicated by the scarcity of reliable official data.[138]

This murky picture aside, the dramatic ramp-up in sanctions during President Mahmoud Ahmadinejad's second term in office (2009-2013) unquestionably surprised the regime.[139] The economy, already mired in an inflationary spiral prompted by government spending, low interest rates and reckless lending, was hit hard.[140] Partly in response, Ahmadinejad implemented a daring reform plan in December 2010 that abolished subsidies on basic staples and energy products.[141] To cushion the blow, the government doled out monthly cash payments approximating $45 per month to 64 million citizens.

Although the policy provided numerous households vital relief, it simultaneously undercut the industrial sector. An economist said, "the removal of subsidies deprived Iranian industries of cheap energy. Poor planning and insufficient resources com-

operation and Development (OECD), 2012, p. 116; Javier Blas, "Iraq's oil output overtakes Iran's", *The Washington Post*, 10 August 2012.

[137] See "Iranian oil revenues 'drop 45%' because of sanctions", BBC, 7 January 2012. For the first time in its history, Iran turned to the private sector to sell a portion of its oil output. The strategy met with only modest success, given the private sector's limited financial resources and long learning curve in establishing contacts and signing contracts under considerable adverse external pressure. Crisis Group interviews, Iranian oil experts, Tehran, Washington, September-December 2012; "بخش‌خصوصی 20 میلیون بشکه نفت صادر کرد" ["The private sector exported 20 million barrels of oil"], Mehr News Agency, 23 October 2012.

[138] Facing what it describes as "economic warfare", the government stopped publishing detailed econometric indicators, which it now considers a matter of national security. "مرکزآمار ایران: آمار تورم محرمانه برای مقامات ارسال می‌شود" ["The Statistical Centre of Iran: Information on inflation rates are confidentially sent to officials"], BBC Persian, 29 August 2012.

[139] Mahmoud Ahmadinejad was elected on a platform of "bringing the oil money to the people's tables". To fulfil this promise, he embarked on a welfare-oriented economic overhaul. A year into his presidency, 50 prominent economists warned that his expansive monetary policy coupled with lower interest rates could "awaken the beast of inflation" and "slow down the country's economic growth". "Iranian economists lash out at Ahmadinejad's policies", Agence France-Presse, 16 June 2006. Former Economy Minister Davoud Danesh-Jafari said, "during my time, there was no positive attitude towards previous experiences or experienced people and there was no plan for the future". See "Ahmadinejad under fire on economy", BBC, 23 April 2008.

[140] According to data from the central bank, imports skyrocketed from $31 billion in 2005 to $62 billion in 2011. At the same time, liquidity increased nearly fourfold, from 700 billion rials to 3.76 trillion rials, prompting a warning by the Supreme Leader. See "مقام معظم رهبري: راهي براي كنترل نقدينگي بيابيد" ["The Supreme Leader: Find a way to control liquidity], "روند نقدينگي در آمار رسمي" ["Liquidity trends according to official statistics"], *Donya-e-eqtesad*, 25 August 2012.

[141] Iran's massive subsidies were estimated to cost about $70 billion, or nearly 20 per cent of GDP, in 2010. The subsidy reform plan, hailed by the International Monetary Fund (IMF), was designed to phase out subsidies by 2015. See Dominique Guillaume, Roman Zytek, and Mohammad Reza Farzin, "Iran – The Chronicles of the Subsidy Reform", IMF, July 2011. The implementation, however, has been a subject of conjecture between Iranian officials and experts. For a critical analysis on implementation of the subsidy reform plan, see "خطاهای هدفمندسازی یارانه‌ها" ["Mistakes of the subsidy reform plan"], *Arman Daily*, 19 December 2012.

pelled the government to jettison the 30 per cent share of the subsidy reform earnings earmarked for industry, instead using it to expand the size of the pool entitled to cash hand-outs".[142] As a result, there was no increase in domestic production to offset the impact of sanctions; instead, supply chains of intermediary goods and raw material were squeezed, further disrupting industrial productivity.[143]

Oil revenue began to shrink in 2012. On 1 March, the Dubai-based Noor Islamic Bank, the single most important channel for oil money repatriation, severed its ties to Iran;[144] two weeks later, SWIFT stopped clearing transactions for blacklisted Iranian financial institutions.[145] With petrodollars stranded abroad, prospects of a hard-currency crisis rattled the nation's foreign exchange markets. The central bank's inadequate response and erratic pronouncements further eroded public confidence in the government's ability to tame market gyrations. An Iranian official admitted: "Between Mahmoud Bahmani [the CBI's governor] and David Cohen [U.S. treasury under secretary for terrorism and financial intelligence], I have a hard time deciding which one has been more harmful to Iran's economy".[146]

Searching for a safe haven for investments, panicked Iranians have rushed to purchase dollars and euros. Over time, propping up the rial became unsustainable. Iran's currency suffered two precipitous plunges, in January and October 2012, losing nearly 80 per cent of its value against the dollar.[147] Strong currency fluctuations

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[142] Crisis Group interview, Iranian economist, Dubai, April 2012.

[143] A factory owner said, "at times, an entire production line has to be shut down because of a missing screw that we can no longer procure because of sanctions". Another entrepreneur explained: "Even when we procure raw materials from an alternative source, quality controls cause months of delay". The government's policy of increasing imports to combat virulent inflation and reducing consumer prices bankrupted many Iranian manufacturing companies unable to compete. Of those that survived some drastically reduced their production, while others opted for mass layoffs. The situation exacerbated Iran's chronic unemployment problem. Crisis Group telephone interviews, Iranian entrepreneurs, Tehran, June-September 2012; Farnaz Fassihi and Jay Solomon, "In Iran's Factories and Shops, Tighter Sanctions Exact Toll", *The Wall Street Journal*, 3 January 2012.

[144] Crisis Group interview, Iranian economist, Dubai, April 2012. Alan Cowell, "Dubai bank says it cut ties with Iranian institutions", *The New York Times*, 29 February 2012; Amir Paivar, "Iran currency crisis: Sanctions detonate unstable rial", BBC, 2 October 2012.

[145] SWIFT managers contend: "There was no option other than obeying regulations of jurisdictions in which we operate (Belgian law). Our reservation over the potential implications of such action was that once our operating principles of trust and political neutrality are overshadowed by external pressure, countries could choose to conduct their financial messages through other means that could be as basic as email or fax, creating a fragmented global financial system". Crisis Group interview, La Hulpe, 4 September 2012. SWIFT's annual report shows that 49 Iranian financial banks and institutions were connected to its network, these transactions accounted for roughly 89 per cent of the country's foreign trade. See "سویفت خدمات خود به بانک‌های ایرانی را متوقف می‌کند" ["SWIFT stops providing services to Iranian banks"], BBC Persian, 15 March 2012. Nearly a dozen Iranian financial institutions that are not blacklisted by multilateral sanctions remain connected to SWIFT. In response, Iran set up a domestic financial messaging system in the summer of 2012. "جزئیات سامانه ایرانی سپام" ["Details on Iran's Sepam Network"], Khabaronline.ir, 1 July 2012.

[146] Crisis Group interview, October 2012. A prominent financier in Tehran described the deep sense of mistrust in the market: "How are we supposed to believe that the government is in control when the central bank announces that in 48 hours the rial's value will be restored or that the exchange rates will be unified, and then nothing happens? Evidence suggests that their coffers are depleting faster than expected. For instance, why did the bank cut travellers' $2,000 currency allowance by half, if they had enough dollar reserves?" Crisis Group telephone interview, Tehran, April 2012.

[147] The open market exchange rate dropped from 10,500 rials per dollar in December 2011 to 41,000 rials in October 2012 before picking up slightly to 37,000 rials in February 2013. The rial has routinely been devalued since the 1979 revolution. (One dollar was worth 70 rials in 1979 and

simultaneously destabilised the business sector. A businessman said, "one can't buy or sell anything, as the rates change every ten minutes. Like an irregular heartbeat, it is debilitating the economy".[148]

Anxiety over potential sanctions-induced shortages pushed both government and households to stockpile staples, which in turn compounded inflationary pressures;[149] annual inflation rose from 12 per cent in October 2010 to 27.4 per cent in December 2012, with peaks in the housing and stock markets.[150] Other indicators followed. According to parliament's research centre, between October 2011 and October 2012, production fell 40 per cent and unemployment grew by 36 per cent, while the price of consumer and primary goods rose by 87 and 112 per cent, respectively.[151] An Iranian business consultant remarked: "The doom and gloom is reminiscent of the war years".[152]

Despite unquestionable hardship, the government – also the single most important economic actor and sole dispenser of petrodollars – enjoys myriad tools to avoid an economic meltdown.[153] In this sense, its efforts have focused far more on adjusting its economy to the reality of sanctions than on seeking their removal. Likewise, whatever lobbying has occurred from key constituencies has been aimed at convincing the regime to amend its economic policies as opposed to its nuclear ones.

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nearly 9,000 rials when Ahmadinejad came into office.) See Arash Hassanya, "سرنوشت ریال ایران از سال ۷۵ تا این روزها" ["The fate of Iranian rial from 1979 to these days"], RFE/RL, 15 September 2012. Some Iranian economists blame the government for artificially propping up the rial and spreading the mistaken belief that a strong national currency symbolises economic vigour and prestige. Others point out that, insofar as the country imports nearly a third of its food, devaluations have devastating consequences on consumer prices. Crisis Group telephone interviews, Tehran, October 2012; Jahangir Amuzegar, "The Rial Saga", Middle East Economic Survey, 6 August 2012. Iran imports 45, 90, and 50 per cent of its consumed rice, cooking oil and sugar, respectively. See "تاثیر نرخ ارز بر قیمت تمام‌شده کالاهای اساسی" ["The impact of currency rate vacillations on the final prices of basic staples"], Mehr News Agency, 5 June 2012.

148 Crisis Group interview, Istanbul, August 2012.

149 Crisis Group telephone interviews, Iranian economists, Tehran, April-October 2012. See also Sarah McFarlane and Michael Hogan, "Iran boosts strategic grain stocks with wheat buy", Reuters, 3 August 2012; "دستور ویژه احمدی‌نژاد برای ذخیره‌سازی/ تامین 3 ماه نیاز کالاهای اساسی" ["Ahmadinejad's special decree for stockpiling three months of essential staples"], Mehr News Agency (in Persian), 27 July 2012.

150 The 2012 inflation rate was the highest official one in the past seventeen years. According to the central bank, the consumer price index increased nearly four-fold since 2005. "بانک مرکزی ایران نرخ تورم در آذرماه را اعلام کرد" ["The CBI Announced the Inflation Rate in December"], BBC Persian, 9 January 2013. Government agencies and economists argue over the accuracy of official economic data. Most experts believe the inflation and unemployment rates to be far higher than those announced by the bank. For more on the unexpected boom in the stock market, see Yeganeh Torbati, "Iran's stock market rally defies economic slump, raises risk of a bubble", Reuters, 12 December 2012.

151 See "مجلس: کاهش ۴۰ درصدی تولید و کاهش ۳۶ درصدی اشتغال در ایران" ["Parliament: 40 per cent drop in production and 36 per cent decrease in employment in Iran"], Entekhab.ir, 25 December 2012. Unemployment, arguably the country's most chronic economic problem, skyrocketed as manufacturing firms shut down or downsized. Iran's automotive industry, which had increased manufacturing fivefold over the prior decade, produced only half as many cars as the previous year. See "تولید خودرو در ایران تقریبا نصف شده است" ["Iran's car production has been cut by half"], BBC Persian, 12 December 2012; Brian Murphy and Nasser Karimi, "Rare labor petition in Iran shows economic alarm", Associated Press, 1 October 2012.

152 Crisis Group telephone interview, Tehran, October 2012.

153 Crisis Group interview, Djavad Salehi Isfahani, Virginia Tech professor of economics, Washington, 10 October 2012; see also his "Understanding the rial's free-fall", Lobelog.com, 4 October 2012.

Accordingly, the government introduced a system of tiered exchange rates;[154] restricted access to preferential rates to ten priority import lists;[155] opened an official exchange centre for licensed importers;[156] cracked down on speculators;[157] and banned the re-export of goods imported under preferential rates.[158] Though criticism of its implementation of such policies has been rife, markets eventually stabilised to some extent as 2012 drew to a close.[159]

After absorbing the initial shocks, the government and business community developed alternative mechanisms for conducting financial transactions. Barter, especially with oil customers, gained traction.[160] Major purchasers of Iranian oil, such as

[154] This was a page stolen from the austere economic policy implemented during the Iran-Iraq war. At the end of the war in 1988, the dollar could be exchanged at twelve different rates. Currently, the market offers three rates: the official rate of 12,260 rials per dollar (used for imports of basic goods such as foodstuffs, pharmaceuticals and agricultural products); the managed floating exchange rate of 25,000 rials per dollar (used by importers of all other goods except luxury items); and the free market rate, determined by supply and demand in officially licensed foreign exchange bureaus. The latter is the smallest of the three but has a significant psychological impact on public perceptions regarding the rial's real value. Crisis Group telephone interview, Bijan Khajehpour, Vienna, 10 October 2012; "Iran introduces tiered exchange rates for imports", Reuters, 21 July 2012.

[155] The central bank issued a list of goods that could be bought at the official rate of 12,260 rials per dollar based on a list of priorities ranking from one to ten. Food and medicine belonged to categories one and two, while industrial intermediate goods came later. The bank also banned the import of 75 so-called luxury goods and prohibited the unlicensed export of some goods, including gold. See Brian Murphy and Nasser Karimi, "Iran bans 'luxury' imports as sanctions bite", Associated Press, 8 November 2012.

[156] The mechanism aimed at exerting greater control over the opaque exchange market; it was introduced following a failed attempt to establish an official currency bourse. However, the centre's inadequate currency supply in its early days triggered another slide in the rial's value. Crisis Group telephone interviews, Iranian traders, Tehran, October 2012; Yeganeh Torbati, "Iran rial plunges as Western sanctions bite", Reuters, 1 October 2012.

[157] Authorities arrested dozens of black market currency traders and threatened speculators with capital punishment. See Rick Gladstone, "Iran reports arresting 50 on money trading violations", *The New York Times*, 24 October 2012; Thomas Erdbrink, "Iran warns currency speculators as rial continues to fall", *The Washington Post*, 1 February 2012.

[158] "Iran bans export of 50 goods as sanctions bite", Reuters, 30 October 2012.

[159] A prominent Iranian businessman said, "the climate of uncertainty is unbearable. As soon as we adjust to new regulations, they are replaced by new directives. Instead of allaying market concerns, these new measures signal abnormality, spurring more psychological distress". Crisis Group telephone interview, Tehran, November 2012. According to a study conducted by the Iranian parliament's research arm, during the summer of 2012 the government shifted its foreign exchange policy on average once every three days. "ارزیابی اقدامات و بخشنامه های بانک مرکزی در حوزه ارزی - فروردین ماه سال 1390 لغایت مهر ماه سال 1391" ["An assessment of the Central Bank's directives and actions with regards to the foreign currency situation between March 2011 and October 2012"], Majles Research Centre, December 2012.

[160] Iran's industry, mining and trade ministry has set up a special barter committee. See Margaret McQuaile, "Iran braces for further sanctions pressure on oil exports", Platts, 11 February 2013. China settles most of its oil debts through barter. Assadollah Asgaroladi, a prominent Iranian exporter, complained that the "whip of sanctions" has left Iran with no option other than bartering with Beijing. "We all like to buy Western products, but because of present conditions we cannot. The United Kingdom could sell us machinery directly instead of selling it through the Chinese, which adds three to four per cent commission to the purchase price. We already have told the Chinese to have no doubt that the day sanctions against Iran are lifted, our cushy relationship will be over". Quoted in *Asseman Magazine*, vol. 20, 21 July 2012. Indian (unlike Chinese) exports to Iran were negligible prior to 2011. New restrictions have changed the equation. India now deposits about 45 per cent of its payments to Iran into an account at the Indian, state-run UCO Bank, which does not have U.S.

India and China, settled accounts in their local currencies;[161] for smaller transactions, *hawala* – an alternative remittance system– replaced banking transactions;[162] for some traders and ordinary citizens, the only way to do business was to physically transport cash.[163]

Sanctions also led Iran to reorient its trading patterns toward Asia, including more immediate neighbours – who, in the words of a European official, "can afford to neither provoke Washington's wrath nor antagonise Tehran".[164] Trade with China soared from nearly $3 billion in 2002 to over $44 billion in 2011;[165] trade relations with India also experienced a boom.[166] Billions of dollars' worth of Iranian products flow into Iraq and Afghanistan. Re-exported U.S. and European goods find their way into Iranian markets via Turkey and the United Arab Emirates (UAE).[167] A shared experience with sanctions has drawn Iran, North Korea and Syria more closely together.[168]

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operations. The money is used by Iranian businesses to pay for the purchase of rice, medicine and steel. Barter is used for the remainder. See Indira Lakshmanan and Pratish Narayanan, "India and China skirt Iran sanctions with junk for oil", Bloomberg, 30 March 2012. Iran and Turkey also engaged in a gold-for-gas swap. Turkey's export of gold to Iran rose from $54 million in 2011 to $6.5 billion in 2012. See "Turkish gold exports rise 800 pct on demand from Iran", Reuters, 4 January 2013; Asli Kandemir, "Turkey to Iran gold trade wiped out by new U.S. sanction", Reuters, 15 February 2013.

161 "بهمنی: طلا و ارز کشورهای دیگر را هم در مبادلات قبول می‌کنیم" ["Bahmani (CBI's governor): We accept gold and other countries' currencies as well"], The Islamic Republic News Agency (IRNA), 28 February 2012.

162 *Hawala* transactions are conducted on the basis of trust and without physically moving funds. Crisis Group observed that whereas business in Iranian *hawala* brokerage houses in Dubai and Istanbul was bustling, it was lacklustre in official Iranian bank offices in those cities. Crisis Group observations; interviews, currency traders, Dubai, Istanbul, April, August 2012. Increased use of *hawala* to skirt sanctions has alarmed the U.S. Treasury Department. See "The Use of Exchange Houses and Trading Companies to Evade U.S. Economic Sanctions Against Iran", OFAC, 10 January 2013.

163 Some Iranian merchants in the UAE transport cash in their luggage, ship it on dinghies across the Persian Gulf or channel it through Oman's banking system and then use trucks for transfer to Dubai. Trustworthy travellers perform the same function for the Iranian diaspora or students studying abroad. Crisis Group interviews, Iranian businessmen, Dubai, April 2012. Truckloads of Iranian rials reportedly are transported to Afghanistan, Iraq and Armenia and then converted into dollars or channelled through their respective financial systems. See Soraya Sarhaddi Nelson, "Can't change your money in Iran? Try Afghanistan", National Public Radio, 28 September 2012; Matthew Rosenberg and Annie Lowrey, "Iranian currency traders find a haven in Afghanistan", *The New York Times*, 17 August 2012; James Risen and Duraid Adnan, "U.S. says Iraqis are helping Iran to skirt sanctions", *The New York Times*, 18 August 2012; Louis Charbonneau, "Iran looks to Armenia to skirt bank sanctions", Reuters, 21 August 2012.

164 Crisis Group interview, Brussels, September 2012.The Iranian government retaliated against European sanctions by imposing an embargo on imports from over 100 European companies. See "قطع واردات از اروپا" ["Imports from Europe halted"], *Donya-e-eqtesad*, 14 April 2012.

165 "Direction of Trade Database", IMF.

166 For India, this has been highly profitable, leading to a surge in exports. See Rick Gladstone, "India explores economic opportunities in Iran, denting Western sanctions plan", *The New York Times*, 9 February 2012; Reza Zandi, "مهم ترین میهمان تهران" ["Tehran's Most Important Guest"], *Shargh*, 6 September 2012.

167 "جزئیات تجارت 9 ماهه ایران" ["Details on Iran's trade during the past nine months"], *Donya-e-eqtesad*, 28 December 2012. With increased restrictions on Dubai-based Iranian firms, many companies have shifted their operations to Turkey. According to Turkish officials, 2,140 Iranian companies were operating in the country at the end of 2011, a 41 per cent increase from 2010. In the first nine months of 2012, an additional 651 Iranian firms established a presence there. See "Number of Iranian-funded firms tops list for ninth month", *Today's Zaman*, 21 October 2012; "UAE exports to Iran

Iranian economists and entrepreneurs widely share the view that the nation's diversified and resourceful economy protects it from imminent collapse.[169] A former official said, "it is a mistake to underestimate Iran's resilience. Not because we have a contingency plan for everything, but because muddling through has been the golden formula for this country's survival over several millennia".[170]

Nevertheless, the loss of nearly half its oil revenue almost certainly will push the government to implement harsher austerity measures. The budget deficit in 2013/2014 is estimated at nearly 40 per cent;[171] although this partly has been offset by currency arbitrage (the foreign currency emanating from oil sales is now worth more in rials), the government has had to slash spending, abandon development projects, plan to increase taxation, consider distributing staple-food coupons and propose an austerity budget for next year.[172] Meanwhile, parliament has halted the second phase of the subsidy reform program, deeming it unaffordable under current circumstances.[173] Although some analysts assert that new economic realities could "empower domestic manufacturing and bolster Iran's non-oil exports",[174] acquiring such capacity at a minimum would be a lengthy and uncertain process.[175] For now, the regime seemingly counts on its foreign currency reserves to buy time and hunkering down.[176]

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slide in first half", *The Wall Street Journal*, 26 December 2012. Iran also signed an agreement with Afghanistan, providing the landlocked country with access to the port of Chabahar. See Joshua Hresh, "Afghanistan's trade deal with Iran complicates U.S. aims", The Huffington Post, 5 September 2012.

168 In October 2012, Iran and North Korea signed a scientific and technological cooperation agreement, while Iran and Syria increased cooperation to overcome their restricted access to fuel. See John Park, "What's Behind New Iran and North Korea Pact", Iran Primer – United States Institute of Peace, 7 September 2012; Jessica Donati, "Iran and Syria swap fuels as both aim to dodge sanction", Reuters, 31 October 2012.

169 Crisis Group interviews, Dubai, Istanbul, Washington, April-December 2012.

170 Crisis Group telephone interview, Tehran, September 2012.

171 "آمار رسمی از کسری بودجه" ["Official statistics on budget deficit"], *Donya-e-eqtesad*, 16 December 2012. The IMF estimates that the Iranian economy shrunk by 0.9 per cent in 2012, while unemployment exceeded 14 per cent. Some economists consider these data to be overly optimistic. Crisis Group interview, Iranian economists, Washington, December 2012.

172 Tax revenues constitute a mere 7 to 8 per cent of Iran's GDP, as roughly 60 per cent of the economy is untaxed. The government plans to double its tax revenues although implementation of required reforms likely will take years. See "درآمد نفتي و فرار مالياتي؛ دو چالش عمده بودجه کشور" ["Oil income and tax evasion, the budget's two main challenges"], *Mardom Salari*, 17 December 2012; "محمود احمدی‌نژاد: بودجه خیلی جاها صفر شده است" ["Mahmoud Ahmadinejad: Many line items of the budget have been zeroed out"], BBC Persian, 9 October 2012. "گام دوم هدفمندی یارانه‌ها در بودجه ۹۲/ کاهش وابستگی به نفت می‌یابد" ["Second stage of subsidy reforms in 92 Budget/Dependence on oil will be reduced"], Fars News Agency, 6 November 2012. "بودجه 92 کل کشور انقباضی است" ["The Budget will contract next year"], Iranian Students News Agency, 28 October 2012; Ladane Nasseri, "Iran may hand staple-food coupons to help poor, Mehr Says", Bloomberg, 24 January 2013.

173 Considering the subsidy reform program as his most important economic legacy, Ahmadinejad favoured its continuation and even acceleration. But given that the first round stoked inflation, parliament voted to stop the program. See Jahangir Amuzegar, "Iran's Subsidy Reform: RIP", Middle East Economic Survey, 14 December 2012.

174 Crisis Group interviews, Iranian economists, Washington, Vienna, November-December 2012.

175 Ahmad Mir-Taheri, "از نفت در سفره‌ها تا اقتصاد بدون نفت" ["From 'oil on the table' to 'oil-less economy'"], *Donya-e-eqtesad*, 23 January 2013. Tightening restrictions on imports of metals and raw material likely will further hurt various industries, including construction, machinery and auto-making. Crisis Group interview, Iranian business consultants, Dubai, Washington, April, November 2012.

176 According to the IMF, Iran's foreign currency reserves stand at $106 billion. It is impossible to verify this amount independently, as Iranian officials regularly provide contradictory estimates. Crisis Group interview, IMF official, Washington, December 2012.

Breaking with its traditional narrative that had derided the international measures as "worthless scraps of paper" and "ridiculous",[177] the regime belatedly began to acknowledge their devastating impact".[178] The new tone arguably was meant to achieve several objectives, principally deflecting popular anger from the government's mismanagement to the West.[179] And not just popular anger: among others, the speaker of parliament, Ali Larijani, called the government's economic stewardship "Robin Hood-ish", faulting the president for 80 per cent of the economic problems and attributing only the remaining 20 per cent to sanctions; in like manner, Friday prayers have seen repeated denunciation of Ahmadinejad's economic stewardship.[180] Paradoxically, then, one could say that "sanctions simultaneously saved and damned Ahmadinejad's presidency",[181] worsening the economic situation even as it provided him with a good excuse for more deeply-rooted (and often self-inflicted) troubles.[182]

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[177] "Ahmadinejad calls U.N. nuke sanctions 'worthless paper'", Associated Press, 11 June 2010. Ahmadinejad's opponents criticise him for his contradictory statements on the impact of sanctions. Despite initially dismissing their effectiveness, the president later blamed them for the country's economic troubles. See, eg, "انتقاد سخنگوی کمیسیون امنیت ملی مجلس ایران از 'کاغذ پاره' نامیدن تحریمها" ["The speaker of the parliament's national security committee criticises dubbing sanctions as scraps of paper"], BBC Persian, 12 October 2012.

[178] These admissions were made first by the president and then by members of his cabinet. See Thomas Erdbrink, "Iran's president says new sanctions are toughest yet", *The New York Times*, 3 July 2012; "Ahmadinejad admits impact of sanctions on Iran", *The Washington Post*, 1 November 2012; "وزیر صنعت و تجارت ایران: تحریم ها فلج کننده است" ["Minister of Industry and Trade: Sanctions are crippling"], BBC Persian, 10 January 2013.

[179] The goal also appeared to be boosting morale by invoking a spirit of resistance. Crisis Group telephone interview, Iranian political analyst, Tehran, October 2012. In the run-up to the March 2012 parliamentary elections, billboards in the capital and other cities equated participation in elections with deterrence against war and sanctions. The claimed 65 per cent turnout rate was portrayed as a testament to popular support for the country's foreign policy. "The participation of Iranians is a great slap in the face of the West", Press TV, 29 February 2012; Robert Worth, "Iran's government declares huge turnout in first national vote since '09 protests", *The New York Times*, 2 March 2012.

[180] See "مشکل تحریم نیست؛ بی تدبیری است" ["The problem is mismanagement, not sanctions"], Fararu.com, 5 October 2012. Critics charged Ahmadinejad with mismanaging the economy and ignoring experts' advice. The president dismantled the planning bureaucracy and other supervisory bodies while side-lining experienced technocrats and experts. Crisis Group telephone interviews, Iranian political analysts, Tehran, April-October 2012. Others argued that his profligate spending and failure to invest in infrastructure left the country more vulnerable to outside pressure. See Mehdi Hassanzadeh, "غفلت هاي ديروز و خسارت هاي امروز" ["Yesterday's Neglect, Today's Damages"], *Khorassan*, 10 November 2012.

[181] Crisis Group telephone interview, December 2012. See also Nasseri, "Ahmadinejad gets blame and sanctions as economy sputters", op. cit.

[182] An Iranian analyst speculated that, "had the country's economic and international situation been less precarious, Ahmadinejad's second term in office would have been curtailed by impeachment". Crisis Group telephone interview, Tehran, April 2012. The Supreme Leader's office instructed parliament to refrain from impeaching the finance minister and probing the president over his handling of the economy "for the greater expedience of the system". See Nasser Karimi, "Iran's parliament drops impeachment over economy", Associated Press, 7 October 2012; Marcus George, "Ahmadinejad off the hook as Iran's parliament withdraws summons", Reuters, 21 November 2012. A European official said, "Khamenei can't afford to sack Ahmadinejad. Internal turmoil under economic siege is a nightmare for the regime". Crisis Group interview, Brussels, October 2012.

D. *Political Impact*

Behind the sanctions policy lies the hope, at least among some of its advocates, that growing popular discontent will confront the regime with a stark choice: altering its nuclear policy or running the risk of popular unrest.[183] A U.S. official summed up this viewpoint: "The regime might be willing to pay a high price for its nuclear ambitions, but for how long are the Iranian people willing to shoulder the cost?"[184]

If that indeed was one of the goals, so far evidence of success is scarce. 2012 witnessed a handful of protests, but these quickly petered out.[185] The appetite for an uprising, with all its attendant sacrifices, appears minimal, arguably a by-product of Iran's own bloody revolutionary past, the fate of the post-2009 election demonstrations and the dark turn taken by the so-called Arab Spring.[186] All in all, a dissident said, "Iranian leaders are not overly concerned about prospects for a 'Tehran Spring'. Their confidence is rooted in part in their successful suppression of the Green Movement in 2009".[187]

To be sure, there are signs of public anger related to the economic downturn. Much criticism is directed at the regime, but there also are indications that the West increasingly is blamed for what is viewed as a form of collective punishment. An Iranian businessman said, "people do not necessarily see a correlation between an increase in the price of domestically-produced goods and sanctions. So they blame the government. But shortages of medicine have changed the dynamics, and people increasingly blame the West for their predicament".[188]

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[183] Some advocates of tough sanctions argue that the fear of bread riots is the only force that could compel the leadership to curtail its nuclear activities. Philip Hammond, British defence secretary, said, "the only thing that is likely to budge the regime is if they see or sense an existential threat. If the level of economic pressure starts to translate into potentially regime-threatening disruption and dissent on the streets of Tehran, then they may change course", quoted in *The Observer*, 6 October 2012; "Turning Iran's Currency Crisis Into a Revolution", editorial, Bloomberg, 7 October 2012.

[184] Crisis Group interview, U.S. official, Washington, February 2013. See also Karen DeYoung and Scott Wilson, "Public ire one goal of Iran sanctions, U.S. official says", *The Washington Post*, 10 January 2012.

[185] Crisis Group telephone interviews, Iranian political analysts, Tehran, July, October 2012. In July 2012, a shortage of imported chicken feed caused poultry prices to soar, prompting protests in the provincial city of Neishabour. In October 2012, after the rial's value plunged, hundreds of angry demonstrators, joined by Bazaar merchants, gathered in front of the central bank chanting, "Leave Syria alone, think of us". In both cases, security forces swiftly dispersed demonstrators. The regime subsequently conducted anti-riot drills in Tehran to demonstrate its resolve to prevent future such incidents. See Hossein Bastani and Ali Hamedani, "Growing anger in Iran over cost of chicken as sanctions bite", BBC, 27 July 2012; Kasra Naji, "Iran police clash with protesters over currency crisis", BBC, 3 October 2012; Rick Gladstone, "West is foolish to celebrate Iran's rial crisis, Ayatollah says", *The New York Times*, 10 October 2012; Farnaz Fassihi, "Grass-roots boycott of bread and dairy shows discontent as sanctions bite", *The Wall Street Journal*, 25 June 2012.

[186] Crisis Group telephone interviews, Iranian civil society and opposition activists, Tehran, Shiraz, October 2012.

[187] Crisis Group telephone interview, Tehran, July 2012. A Revolutionary Guards commander said, "[Our] assumption is that unrest may break out in smaller cities, away from Tehran. Livelihood difficulties and the vulnerability of the working class are the factors that can spark the unrest, however, we have sufficient experience of dealing with it". Quoted in "پیش‌بینی یک فرمانده سپاه: ناآرامی این‌بار از شهرستان‌ها شروع می‌شود" ["Prediction of an IRGC commander: Unrest is likely to start from provinces"], BBC Persian, 14 January 2013.

[188] Crisis Group interview, Iranian entrepreneur, Istanbul, August 2012. An Iranian dissident complained: "The West has been dishonest about the objectives of its pressure policy. On the one hand, its leaders say that they don't want to hurt ordinary Iranians, but on the other hand, their ostensible

Important regime constituencies have been harmed by international penalties, but not all of them and, here as well, not in a manner that translates into pressure on Tehran to adjust its stance on the nuclear file.[189] Despite a significant privatisation effort, governmental and semi-governmental institutions still dominate the economy. Evidence suggests that, although decreased oil revenues have adversely impacted nearly all key stakeholders, groups with better contacts with the state have been in a position to weather the storm, find ways to circumvent sanctions, exploit new opportunities and thus minimise damage to their interests.[190].

Even as economic hardships – at least partially triggered by sanctions – provoked intense regime infighting,[191] such disagreements have yet to touch upon the policy at the root of the sanctions, namely continuation of the nuclear program and insistence on Iran's right to enrich. After nearly a decade of public posturing, the nuclear issue politically has become virtually untouchable. An Iranian analyst noted:

> Even the more moderate political currents chiefly criticise the tone, not the core, of Iran's nuclear policy. Almost every leader in the past five decades, independent of his character and ideological belief, from the Shah to reformist and conservative presidents, has been involved in the nuclear program. Short of some face-saving strategy, there is little doubt that the leadership will continue along the same path.[192]

Attention is focused far more on how best to side-step (or, in some cases, benefit from) sanctions through manipulation of economic policy than on how to end them through revision of nuclear policy. Indeed, the sense of encirclement potentially could trigger a more belligerent stance in that respect. According to a former Iranian nuclear negotiator, "the siege mentality appears to have bolstered radicals within the political elite who argue that since sanctions have already exacted the same price as would be inflicted in the event Iran acquired a nuclear weapon, this final step should be taken".[193]

goal is to ensure that economic dissatisfaction reaches boiling point and magically resolves their problems with the Islamic regime". Crisis Group telephone interview, Tehran, November 2012.

[189] Crisis Group telephone interviews, Iranian political activists, Tehran, Vienna, Boston, May-November 2012.

[190] Crisis Group telephone interviews, Iranian economists, Tehran, April-December 2012. A similar phenomenon occurred during the Iran-Iraq War, when revolutionary and religious foundations under the Supreme Leader's direct control – such as the Foundation of the Oppressed and War Veterans – morphed into giant conglomerates, reportedly controlling nearly a quarter of Iran's economy. See David Thaler, Alireza Nader, Shahram Chubin, Jerrold Green, Charlotte Lynch, and Frederic Wehrey "Mullahs, Guards, and Bonyads", Rand Corporation, National Defense Research Institute, 2009.

[191] Some parliamentarians accused the president of deliberately sabotaging the currency market for political goals. "آشفتگی بازار ارز عمدی است" ["Turmoil in the exchange market is intentional"], Mehr News Agency, 30 September 2012. An editorial at a daily newspaper with close ties to the Supreme Leader argued: "The president cannot employ these tricks to mask his government's shortcomings, especially given that his government enjoyed the highest level of support and had the highest oil income in the country's history". "این حنا دیگر رنگي ندارد" ["This henna has no more colour"], *Jomhouri-e-Islami*, 12 November 2012.

[192] Crisis Group telephone interview, Tehran, October 2012.

[193] Crisis Group interview, Hossein Mousavian, Princeton, 6 January 2013.

E. *Unintended or Unforeseen Consequences?*

Officially, Western policymakers argue that the economic penalties are finely tuned, "smart" sanctions aimed at the political elite rather than ordinary citizens.[194] Yet, as sanctions gradually snow-balled – the measure of success increasingly becoming their comprehensiveness, harshness and ability to wreak havoc on the economy – and broad-based punishments gradually superseded more "targeted" ones, their impact likewise broadened, affecting nearly all aspects of life, inflicting long-lasting social harm and fuelling popular criticism of Western policy. Seizing on this, Mohammad Reza Fayyaz, Iran's ambassador to the UAE, claimed that the West's ulterior motive is "to harm the Iranian people and sanction them to the point that it produces social upheaval".[195]

As seen, and as often is the case with sanctions, members of the elite with greatest access to the regime and state privileges are best positioned to survive and even thrive in the new environment. The multiple-exchange-rate system and distribution of subsidy stipends provide segments of the ruling apparatus with potent patronage tools to purchase loyalty and protect core constituencies.[196] The IRGC and state-affiliated enterprises generally have benefited most by virtue of privileged access to favourable currency rates.[197] By contrast, the more vulnerable category of citizens with least connections to the regime has been least capable of circumventing their effects, finding substitute sources of prohibited goods or capitalising on scarcity to boost profits. Unsurprisingly, opposition leaders and human rights activists consistently have opposed broad-based sanctions.[198]

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[194] Then-U.S. Secretary of State Hillary Clinton said, "[our] goal is to pressure the Iranian Government, particularly the Revolutionary Guard elements, without contributing to the suffering of the ordinary Iranians who deserve better than what they currently are receiving". U.S. Department of State, 4 January 2010.

[195] Crisis Group interview, Abu Dhabi, 19 April 2012.

[196] The currency exchange centre has magnified the regime's leverage vis-à-vis a private sector that already was stagnating. Likewise, uneven distribution of subsidy hand-outs and selective tax collection give the regime the option of directing economic pressure on upper- and middle-income citizens, generally considered friendlier towards the West and least prone to revolt. Crisis Group telephone interviews, Iranian economists, Tehran, October 2012; see also Djavad Salehi-Isfahani, "With Friends Like These", *Foreign Policy* (online), 12 October 2012.

[197] An Iranian businessman complained: "The wrong people are benefiting. Anyone with IRGC ties can easily obtain a letter of credit at the official currency rate of 12,260 rials to the dollar. He can then turn around and sell on the open market at double or triple that price". Crisis Group interview, Istanbul, August 2012. In reality, it would be wrong to lump the entire IRGC together; the situation is more nuanced. Crisis Group telephone interviews, Iranian economists and political analysts, Tehran, October-December 2012. An analyst said, "the IRGC is an amorphous and opaque organisation. It has hundreds of subsidiaries. There also are other religious and charitable organisations. It is not obvious who has most profited and who has most suffered as a result of the economic context". Crisis Group telephone interview, Farideh Farhi, Honolulu, 28 December 2012.

[198] Hadi Ghaemi, director, International Campaign for Human Rights in Iran, said, "the reason Iran's human rights community is opposed to comprehensive sanctions is that they hurt average Iranian citizens more than the regime. The middle class is the engine of change and advocacy for political opening; but sanctions ensnare them with economic survival and thus weaken movements for human rights and democracy". Crisis Group telephone interview, New York, 18 December 2012. Inside Iran, opposition leaders have adopted a similar position vis-à-vis comprehensive sanctions. See Thomas Erdbrink, "Iranian opposition warns against stricter sanctions", *The Washington Post*, 1 October 2009.

Examples abound. Students facing banking restrictions and the rial's devaluation find it ever more difficult to pay their tuition; some have been compelled to abandon their studies because they did not enjoy access to subsidised currency rates or because their families no longer could support them.[199] Among this category, women have been more disadvantaged still, disproportionately affected by the sanctions. With an economy in recession, they have seen educational and career opportunities evaporate at much faster rates than men.[200]

Arguably the most negative consequence has been to seriously undercut the healthcare system.[201] These problems are compounded by the rial's depreciation, which dramatically jacked up the price of imported and domestically-produced medicine and deepened the crisis.[202]

Reports of widespread shortages of specialised medicines for cancer patients, haemophiliacs and individuals suffering from diabetes, multiple sclerosis and other serious conditions are numerous.[203] Although the healthcare sector is largely self-sufficient, it still depends on importation of key ingredients and patent-protected drugs.[204] True, U.S. and EU sanctions exempt medicine, food and humanitarian aid

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[199] Crisis Group interviews, Iranian students, Washington, Brussels, Boston, April-November 2012; see also "تصمیم وزارت علوم برای دعوت از دانشجویان بورسیه خارجی به داخل کشور" ["Decision by the Science and Education Ministry to request students studying abroad on government scholarships to return to the country"], Mehr News Agency, 29 September 2012; Yeganeh Torbati, "Iranian students feel the pain as currency collapses", Reuters, 17 October 2012.

[200] For a review of the effects of sanctions on Iranian women, see "Killing them Softly: The Stark Impact of Sanctions on the Lives of Ordinary Iranians", International Civil Society Action Network, July 2012.

[201] Shortages of medicine and medical equipment, although triggered by sanctions, were aggravated by the government's overall unpreparedness. It did not stockpile essential active pharmaceutical ingredients and specialised medicines; see Mohammad-Hussein Nejati, "عضو کمیسیون بهداشت و درمان مجلس: تنها برای دوماه آینده ذخیره دارویی داریم" ["A member of Iranian parliament's healthcare committee: We only have two months' worth of drug reserves"], Khabaronline.ir, 10 November 2012; failed to set aside sufficient foreign currency, see Khabaronline.ir (in Persian), 14 December 2012; and did not reimburse pharmacies in a timely fashion, thus prematurely depleting their financial resources. Crisis Group telephone interviews, Iranian pharmacists, Tehran, Shiraz, Mashhad, August 2012.

[202] Deans of medical schools across Iran warned of exceedingly high prices for medicine and medical equipment. "هشدار دانشگاه‌های پزشکی ایران در مورد افزایش ۰۵۳ درصدی قیمت دارو" ["Warning from Iran's medical universities regarding the 350 per cent increase in the price of medicine"], BBC Persian, 11 November 2012. Information about daily price increases of specialised medicine, posted by one of Tehran's main pharmacies, can be accessed at www.13abanpharmacy.com/?status=newdrugs. Fear of shortages and future price spikes pushed patients to stockpile medicine at home, further exacerbating the crisis. Some pharmacies were forced to ration their supplies to prevent such behaviour. Crisis Group telephone interviews, Iranian pharmacists, Tehran, October 2012.

[203] Shortages reportedly have affected specialised medicines and even common drugs, such as birth control pills and anaesthetics. See Golnaz Esfandiari, "Iranian media say sanctions taking toll on seriously ill patients", Radio Free Europe, 15 October 2012. Some hospitals have been forced to resort to archaic anaesthetic techniques, using chloroform for minor surgeries. Crisis Group telephone interview, director, private hospital, Shiraz, November 2012; "داروهای بیهوشی کمیاب شدند" ["Anaesthetic medication becomes rare"], Fars News Agency, 9 November 2012. For a list of 50 imported drugs missing or in short supply, see "اسامی ۰۵ قلم داروی نایاب در ایران" ["The name of 50 scarce drugs in Iran"], Tejarat Farda Weekly (in Persian), 13 October 2012.

[204] Marzieh Vahid-Dastjerdi, former health minister, asserted that 96 per cent of the country's medicine and 85 per cent of its medical equipment is domestically manufactured; even so, Iran annually imports an estimated $2.5 billion worth of specialised drugs, modern medicine and active pharmaceutical ingredients. See "تحریم نبودن داروی ایران یک دروغ بزرگ است" ["The exemption of Iran's

as their officials consistently and correctly emphasise.[205] But the broad financial restrictions have gone a long way toward neutralising such waivers.[206] Seeking to address the problem, the U.S. Treasury Department issued a "standing authorization", allowing U.S. companies to sell certain medicines and supplies without a licence;[207] in the same spirit, Germany instructed its banks to process payments for exports of medicine to Iran.[208] Yet, these efforts so far seemingly have failed to yield meaningful results. Foreign banks remain reluctant to do business with Iran for fear of running afoul of the complex web of sanctions.[209] Steering clear of business with Tehran is the path of least resistance.

Iranian importers of medical products face daunting challenges. Obtaining letters of credit itself is a major obstacle course. An Iranian importer said:

> Most importers are now applying for letters of credit through Turkey's Halk Bank. The U.S. tolerates this narrow channel. But the problem is that Halk Bank no longer is willing to open new accounts for Iranian customers, as demand has peaked and waiting periods for approving funds have become excessively long. To make matters worse, before recent restrictions we used to put down around 30 per cent

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pharmaceutical imports is a big lie"], Fars News Agency, 25 October 2012. The rapidly deteriorating situation led many prominent Iranians to express concern. The director of Iran's Haemophilia Society wrote: "This is a blatant hostage-taking of the most vulnerable people by countries claiming to care about human rights. Even a few days of delay [in obtaining medicine for haemophilic patients] can have serious consequences like haemorrhage and disability". Quoted in Najmeh Bozorgmehr, "In Iran, sanctions take toll on the sick", *The Washington Post*, 4 September 2012. Fatemeh Hashemi, daughter of former President Rafsanjani and head of Iran's Foundation for Special Diseases, wrote to the UN Secretary-General: "Although medicine has not been sanctioned, due to the impossibility of paying for the imported drugs through the banking system, the heavy shadow of the sanctions is felt in the health sector. Not only have the imports of medicine been disrupted, but importing raw chemicals [for drugs that are domestically produced in Iran] has been equally interrupted". See "نامه فاطمه هاشمی به بان کی مون" ["Fatemeh Hashemi's letter to Ban Ki-moon"], Iran's Foundation for Special Diseases, 14 August 2012.

[205] Crisis Group interview, U.S. official, Washington, February 2013.

[206] Iran's imports of medicinal and pharmaceutical products from the U.S. and EU dropped by more than 50 and 30 per cent, respectively. See Arshad Mohammed, "U.S. pharmaceutical exports to Iran cut in half in 2012", Reuters, 8 February 2013; Fariba Sahraei, "تحریم و دارو: درد بی درمان" ["Sanctions and Medicine: The Incurable Illness"], BBC Persian, 19 January 2013. According to the UN Secretary-General, "even companies that have obtained the requisite license to import food and medicine are facing difficulties in finding third-country banks to process the transactions". Quoted in Michelle Nichols and Louis Charbonneau, "U.N. chief says sanctions on Iran affecting its people", Reuters, 5 October 2012.

[207] Critics argue that the list comprises only the most rudimentary medical supplies, such as needles, syringes, canes and thermometers. Concerned about dual-use products, U.S. Treasury Department officials have been loath to expand the list to cover more vital drugs. Crisis Group interviews, Washington, 13 December 2012. See list of exempted medical products at www.treasury.gov/resource-center/sanctions/Programs/Documents/med_supplies_10222012.pdf.

[208] "Banken sollen Geldgeschäft mit Iran ermöglichen", *Frankfurter Allgemeine Zeitung*, 2 December 2012.

[209] A U.S. sanctions expert said, "for many years, U.S. Treasury officials sought to dissuade third-country financial institutions from doing business with Iran. Now, administrative burdens and risks of doing business with Iran have increased to a level that even having a Treasury license does not change the big picture". Crisis Group interview, Washington, September 2012. A Tehran-based European ambassador said, "despite our government's carte blanche, the pharmaceutical industry does not want to have anything to do with Iran, and we are unable to force them to do so". Crisis Group interview, Washington, October 2012.

> of the value to open a credit line; now advanced payment of the full amount, if not more, is mandatory given currency fluctuations and uncertainties.[210]

Substituting alternative sources for traditional U.S. and EU medicine suppliers is an unworkable solution, at least in the short to medium term.[211] Plus, there are wholly unplanned consequences that adversely affect Iran's political economy. Among these, smugglers of counterfeits as well as black market operators have seized the opportunity to maximise their profit. An exporter of pharmaceutical products to Iran said:

> There is a mafia in Iran's pharmaceutical industry, composed of quasi-governmental and state-owned companies. They use their connections to register drugs that may be of lower quality, obtain favourable currency rates for their imports and sell them at much higher prices in the open market. I work in other regional countries, but I have not seen this level of corruption anywhere else.[212]

Sanctions also have come at the expense of aviation safety. A U.S. ban on the purchase of aircraft and spare parts has prevented Iran from upgrading its worn-out fleet, arguably a key factor in the unusually high number of airplane accidents.[213] The logic behind these restrictions escapes most Iranians.[214]

Likewise, the diaspora faces particular problems. It is unsure how to send remittances and donations to Iran-based charities[215] and has to deal with both abrupt closings of bank accounts and intrusive questioning at border crossings.[216] Then there

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[210] Crisis Group interview, Iranian pharmaceutical importer, Dubai, 18 December 2012. Even if funds are obtained and imports paid for, shipment of products is fraught with other problems. A regional representative of a European pharmaceutical company said, "We can't ship our products to [Iran's main port] Bandar Abbas any more. We have to declare the final destination of the chemicals as Dubai and then re-ship from there. We have to assure the Emirati officials that our products are not dual-use. In the meantime, we have to store our products in the UAE. All of these steps entail additional costs, which increase the final price by 40 to 80 per cent". Crisis Group interview, Dubai, 20 December 2012.

[211] Mere registering of new formulas often requires completing a lengthy bureaucratic process. Moreover, drugs from India, Bangladesh and China are said to tend to be of inferior quality. Crisis Group interview, Iranian importer, Dubai, December 2012.

[212] Crisis Group interview, Dubai, 20 December 2012.

[213] These prohibitions were imposed during the Clinton administration. Although the Bush and Obama administrations allowed the sale of spare parts necessary for the safe operation of civilian U.S.-made aircraft upon receiving an OFAC licence, the 2012 designation of nearly all major Iranian airlines for alleged involvement in arms transfers to Syria in practice appears to have nullified those prior authorisations. See Katzman, "Iran Sanctions", op. cit.; Bradley Klapper, "US lists 117 Iranian planes arming Syria's Assad", Associated Press, 19 September 2012. Iran's airline accident rate is nearly 40 times higher than North America's; over 1,000 Iranians have lost their lives in fatal aircraft accidents since 1996. See aviation-safety.net/database/dblist.php?Country=EP.

[214] Thomas Erdbrink, "Iran's aging airliner fleet seen as faltering under U.S. sanctions", *The New York Times*, 14 July 2012.

[215] After the 2003 and 2012 earthquakes, the U.S. Treasury Department issued a temporary general license for relief organizations and extended it several times. Although the licence was effective in 2003, in 2012 most financial institutions – notwithstanding it – shunned transferring monetary aid to stigmatised Iranian banks. See Josh Rogin, "Obama administration allows earthquake relief money for Iran", *Foreign Policy* (online), 22 August 2012.

[216] A Prague-based Iranian entrepreneur said, "financial sanctions are taking a toll on ordinary Iranians. My bank accounts were closed in the Czech Republic. When I asked the authorities to show me the relevant clauses in the sanctions legislation, they were dumbfounded. They had no idea. For me as an Iranian citizen without any government affiliation, this behaviour represents plain hypocrisy". Crisis Group telephone interview, Prague, November 2012. For a review of how sanctions

is civil society and the cultural sphere: activist groups, already facing harsh government repression, have seen their limited financial resources dry up; restrictions on the export of communications technology from the U.S., besides impeding the regime's electronic surveillance of its citizens, also has hindered the flow of information;[217] independent publishing houses have gone bankrupt; and funding for artistic activities is shrinking.[218]

Iran's economic predicament – whether caused or aggravated by sanctions – also risks creating a deleterious social climate that is unlikely to be in either the West's or the Iranian people's longer-term interests. Crime rates and corruption have been rising;[219] and smuggling is booming as clandestine networks replace commercial ones.[220] Indeed, smuggling networks are becoming an integral part of the shadow economy that reportedly accounts for 21 per cent of GDP.[221] This does not neces-

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have affected Iranians in the U.S., see, "Unintended Victims: The Impact of the Iran Sanctions on Iranian Americans", joint venture by the Asian Law Caucus, the Iranian American Bar Association, the National Iranian American Council and the Public Affairs Alliance of Iranian Americans, November 2012.

[217] In March 2012, President Obama said, "technologies that should empower citizens are being used to repress them. Because of the actions of the Iranian regime, an electronic curtain has fallen around Iran – a barrier that stops the free flow of information and ideas into the country, and denies the rest of the world the benefit of interacting with the Iranian people, who have so much to offer". Quoted in Matt Spetalnick, "Obama assails Iran's 'electronic curtain' in video message", Reuters, 20 March 2012. Congress recognised the counter-productive impact of sanctions in this area and added waivers. By subsequently granting a general licence, the Obama administration also relaxed restrictions on mass-market personal communications software and services. Opposition members complain that these steps are insufficient; they advocate extending exemptions to more software and hardware technologies. Crisis Group interview, Ali Akbar Mousavi-Khoeini, former chairman, Iranian parliament's communication technology committee, Washington, 15 November 2012. U.S. officials remain cautious given the ambiguous world of dual-use technologies. Crisis Group interview, U.S. official, Washington, December 2012. See also James Ball, "Sanctions aimed at Syria and Iran are hindering opposition, activists say", *The Washington Post*, 14 August 2012.

[218] "When you have to moonlight, you simply cannot afford to ponder issues of democracy and human rights". Crisis Group telephone interview, Tehran, July 2012. Also see "Media Analysis: Paper Prices and Unintended Consequences: How Sanctions Have Limited Access to Independent Publications in Iran", Iran Media Program, 16 October 2012; Sune Engel Rasmussen, "Iranian artists hit by sanctions", *The Guardian*, 22 January 2013.

[219] According to the police, burglaries increased by 9 per cent between March 2011 and March 2012. "میزان کشفیات جرم سرقت در سال 90 در مقایسه با مدت مشابه، 9 درصد افزایش یافته است" ["Detection of robberies in year 1390 increased 9 per cent in comparison to last year"], Police.ir, 6 May 2012. An Iranian businessman said, "you have to pay kickbacks at every turn. There was corruption in the past, but now it is endemic". Crisis Group interviews, Istanbul, August 2012.

[220] The value of smuggling reportedly increased by 58 per cent between 2011 and 2012. About 80 per cent of mobile telephones sold in Iran, 90 per cent of imported clothing and 40 per cent of household appliances were brought in illegally in 2011. "رشد 58 درصدی ارزش کالاي قاچاق کشف شده" ["58 per cent increase in seized smuggled goods"], *Donya-e-eqtesad*, 6 September 2012. The speaker of Iran's parliament estimated the total value of smuggling at some $18 billion and accused influential and intelligence officials of benefiting. See "٨١میلیارد دلار قاچاق کالا در کشور مطرح است" ["$18 billion of smuggled goods in the country"], Khabaronline.ir, 7 January 2013.

[221] Opportunities for corruption have increased exponentially. According to an expert on Iran's shadow economy, "the tiered exchange rate system creates impetus for corruption. Mis-invoicing allows traders to profit from selling some of the currency obtained at preferential rates on the black market. Price disparity also creates incentives for smuggling. The rial's depreciation has cancelled the subsidy reform's price correction and encouraged smuggling of Iran's gasoline and other energy products to neighbouring countries". Crisis Group telephone interview, Mohammad Reza Farzanegan, professor of economics, Philipps University, Marburg, 9 January 2013; see also Ladane Nasseri

sarily harm the regime. To the contrary: it has facilitated a symbiosis between state-affiliated organisations such as the IRGC and transnational smuggling networks.[222] Over time, organised crime networks likely will become more sophisticated, enabling them to survive even after sanctions have been lifted.[223] Iran's proximity to two countries rating highest on the corruption scale – Iraq and Afghanistan – likely contributes to cross-border criminality, undermining longer-term regional stability.[224]

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and Yeganeh Salehi, "Iranian smugglers feel the pressure as sanctions bite", Bloomberg, 26 June 2012; "سهم 21 درصدي اقتصاد پنهان" ["The shadow economy's 21 per cent share"], *Donya-e-eqtesad*, 6 September 2012.

[222] In July 2011, President Ahmadinejad implicitly accused the IRGC of operating jetties for illegal imports. He said that the market for smuggled cigarettes created billions of dollars in illicit profit and attracted not only international criminals but also "our own smuggling brothers". See www.youtube.com/watch?v=XxusPYQ50Is. The IRGC's commander, General Mohammad Ali Jafari, denied the charge. See "مبادلات تجاری در اسکله‌های سپاه انجام نمی‌شود" ["The IRGC's dockyards are not used for commercial activities"], Mehr News Agency, 2 July 2011.

[223] In the words of a sanctions expert, "smuggling is learning by doing". Crisis Group interview, Brussels, 4 September 2012. See also Joby Warrick, "In Iran, drug trafficking soars as sanctions take bigger bite", *The Washington Post*, 1 November 2012; Peter Andreas, "Criminalizing Consequences of sanctions: Embargo Busting and Its Legacy", *International Studies Quarterly*, vol. 2205, no. 49 (2005), pp. 335-360.

[224] In 2012, Iraq and Afghanistan ranked 169 and 174, respectively, on the corruption perception index list of 174 countries surveyed by Transparency International.

IV. An Unsuccessful Success?

A. *A Vicious Cycle?*

Despite the considerable toll sanctions have exacted on Iran's economy, so far they have failed to achieve their proclaimed core objective: to influence Iran's behaviour on the nuclear file. This hardly is surprising. Critical differences exist between how policymakers in Washington and Brussels on the one hand and Tehran on the other view and interpret the sanctions regime.

To begin, while the West views it as an instrument of coercive diplomacy, primarily designed to pressure Tehran into curtailing its nuclear activities – and abandoning any military pursuit in that field – Iran sees it, and indeed the nuclear issue as a whole, as a thinly disguised pretext to undermine the regime. U.S. and EU officials claim that sanctions "lay bare to Iran's leadership the fact that ignoring the international community's demands will result in real and crippling penalties";[225] conversely, they prove that "if Iran acts responsibly, it can bring sanctions to an end".[226] In response, Iranian officials point out that economic pressure predates the nuclear issue; they have been a "primary and permanent feature of U.S. policy towards Iran"; and "since the West's problem is with the Islamic Republic's fundamental tenets, Iran is damned if it cooperates and damned if it does not".[227]

By the same token, the belief in Washington and Brussels that Tehran might surrender to pressure stands in sharp contrast to Iran's self-perception. Western officials who believe crippling sanctions might force the Islamic Republic to rethink its calculations routinely invoke well-known historical precedents – in 1988, despite his "war, war, till victory" slogan, Ayatollah Khomeini "drank the poisoned chalice" and accepted to end the essentially stalemated eight-year war with Iraq; then, in 2003, in the wake of the U.S. invasion of Iraq, Tehran agreed to suspend uranium enrichment and purportedly offered a grand bargain to Washington. The conclusion drawn from these rare policy reversals tends to be clear: faced with an existential threat to the regime, Iran will budge.[228]

Yet, there are good reasons to believe that 2013 is akin neither to 1988 nor to 2003. The decision to end the war in 1988 certainly was a painful one, but from the Supreme Leader's vantage point, it was a step that would ensure the Islamic Republic's survival. By contrast, a compromise on the nuclear file delivered under pressure to an entity (the U.S.) whose goal is believed to be regime change might do nothing of the sort. Compliance with Western demands, in Ayatollah Khamenei's mind, likely will not result in alleviation of pressure.[229] Today's calculus, in other words, is not so clear-cut: a concession risks projecting weakness both domestically and internationally and thus damage prospects of regime survival rather than enhance it. Under this view, the deal, not its absence, could be the poison that brings down the Islamic Re-

[225] Crisis Group interview, U.S. official, Washington, May 2012.
[226] Crisis Group interview, senior EU official, Brussels, May 2012.
[227] Crisis Group interview, Iranian official, December 2012.
[228] Crisis Group interviews, U.S. officials, Washington, May, November 2012; EU officials, May, September 2012.
[229] Crisis Group telephone interview, former Iranian diplomat, Tehran, February 2013; also, Trita Parsi, "The U.S. and Iran's mistaken path to war", The Huffington Post, 20 June 2012.

public.[230] Finally, contrary to the conventional wisdom, the 2003 offer was an invitation to the U.S. for discussing major issues of contention and not an Iranian commitment to unilaterally and unconditionally reverse course.[231]

Moreover, and importantly, for many in the Iranian leadership current hardships have an air of déjà vu – indeed, an air of something not nearly as bad as what previously has been seen. The country has experienced two oil embargos in its modern history: the British-led boycott of Iranian oil between 1951 and 1953 (after Iran nationalised its oil industry) proved highly effective, yet Prime Minister Mohammad Mossadegh did not budge;[232] later, the U.S. embargo on Iranian oil imposed in the wake of the 1979 hostage crisis likewise failed to meet its objective, as American diplomats remained in captivity for 444 days.[233]

Iran also has dealt with two foreign currency crises in the recent past. Oil revenues dropped from $21 billion in 1983 to $6 billion in 1987, at a time when the country was engaged in a full-fledged war with Iraq. A decade later, amid the Asian financial crisis, oil income fell once more, from $19 billion in 1996 to $10 billion in 1998.[234] The situation today – despite shrinking resources and rising prices — is nowhere near the deprivation experienced during the 1980s, when the drain of war had caused widespread shortages and frequent blackouts. Ayatollah Khamenei, who presided over these previous crises, first as president and then as Supreme Leader, said:

> [The] challenges the Islamic Republic is currently faced with are not new. And this is not an analysis, it is a fact. ... There was a day when our ships and oil tankers were targeted in the Persian Gulf. There was a day when [Iraq] bombed our main

[230] Crisis Group telephone interview, former Iranian official, Tehran, February 2013; see also Crisis Group Report, *In Heavy Waters*, p. 26, op. cit. Some Iranians argue that, insofar as Iraqi forces by then had been pushed off Iranian soil, the 1988 ceasefire agreement allowed Tehran to save face and claim victory. See Hossein Mousavian and Mohammad Ali Shabani, "How to talk to Iran", *The New York Times*, 3 January 2013.

[231] The unsigned Iranian letter was both faxed to the U.S. Department of State and sent to the White House through the Swiss ambassador to Iran (Switzerland represents U.S. interests in Tehran) purportedly offering to stop supporting Lebanese and Palestinian militant groups, cooperation with the U.S. in Iraq and Afghanistan and increased nuclear transparency, in return for Washington ending its hostility, repealing all sanctions and disbanding the Iranian rebel group the Mujahedin-e-Khalq. The original draft of the so-called grand bargain rejected by the Bush administration is available at www.nytimes.com/packages/pdf/opinion/20070429_iran-memo-expurgated.pdf. Ayatollah Khamenei insists that Iran's interest in negotiations is not driven by external pressure. He recently stated: "Contrary to Western lies, we had never abandoned the negotiating table on issues, including the nuclear issue, to then return to it". Quoted in "رهبرانقلاب: ما میز مذاکره را ترک نکرده بودیم که بازگردیم" ["The Leader of the Revolution: We had never left the negotiating table to return to it"], Entekhab.ir, 16 October 2012.

[232] The standoff ended with a coup d'état that toppled Mossadegh's government. See Mark J. Gasiorowski and Malcolm Byrne (eds.), *Muhammad Mosaddeq and the 1953 Coup in Iran* (New York, 2004); and Christopher de Bellaigue, *Patriot of Persia: Muhammad Mossadegh and a Tragic Anglo-American Coup* (New York, 2012).

[233] See Suzanne Maloney and Ray Takeyh, "The Self-Limiting Success of Iran Sanctions", *International Affairs*, vol. 87, November 2011.

[234] Iran's oil sales (1959-2010), Central Bank of Iran. Data at www.cbi.ir/simplelist/4454.aspx. In both cases, Iran responded by adopting harsh austerity measures and drastically cutting imports. Tehran appears to have taken a page from its old playbook, cutting imports by nearly $5 billion in the first nine months of its fiscal year (March 2012 to March 2013). See Patrick Clawson, "Will Iran Weather the Economic Storm?", *Foreign Policy* (online), 11 October 2012; "افت نزدیک به ۵ میلیارد دلاری واردات ایران" ["Iran's imports fell by enarly $5 billion"], BBC Persian, 4 January 2013.

> oil terminal in Kharg Island. There were days when the enemy used to drop bombs on all our industrial centres. These are the things that we have witnessed with our own eyes. We have experienced these things before: they are not new to us.[235]

In response, U.S. and EU officials occasionally argue that the more recent round of sanctions is unprecedented in scope and thus should be given enough time to "sink in".[236] They see the accumulated impact of punitive measures, not the effect of their periodic intensification, as the force that eventually might compel the regime to alter its stance in fundamental ways. A senior U.S. official said, "when we think about the impact of sanctions on Iran's oil and gas sector, we think long-term. Imagine what will happen five to ten years from now, when Iranians cannot even keep up oil production for their domestic consumption".[237] Yet, the Iranian leadership offers a mirror image, persuaded that time is on its side. An official argued: "The West will realise in due course that strong-arming Iran is an exercise in futility. But even if it doesn't, fatigue will eventually set in, and the sanctions regime will start haemorrhaging".[238]

To this end, Iran is preparing itself for a potentially prolonged confrontation. At the core of its strategy is its so-called "economy of resistance",[239] which equates survival with victory.[240] From this perspective, dissuading its foreign foes from toppling it and establishing the fact of regime endurance is well worth suffering such costs.[241]

Iran and the West may be sitting at the same chessboard, but they are playing according to entirely different rules. The result at times appears akin to a vicious cycle. In an effort to pressure Iran, the West tightens its sanctions; for the above-described reasons and in order to prove it will not give in to threats, Tehran does not respond according to plan; this in turn prompts ever-tightening sanctions whose success is measured less by their self-proclaimed political goal (to halt Iran's nuclear program)

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[235] From "Ayatollah Khamenei's speech to government officials", Khamenei.ir (in Persian), 24 July 2012. In recent times, the Supreme Leader has used economic themes to name Persian calendar years (such as the year of "economic jihad" or the year of "national production and supporting Iranian labour and capital").
[236] Crisis Group interview, U.S. officials, Washington, June 2012, February 2013.
[237] Crisis Group interview, Washington, May 2012.
[238] Crisis Group interview, Iranian official, October 2012. This perception has been reinforced by recent rulings of the EU General Court that lifted EU sanctions on some Iranian banks. Crisis Group telephone interview, Tehran, February 2013. The court found that the EU Council had failed to provide sufficient evidence that Bank Saderat and Mellat were involved in Iran's nuclear program. The Council has two months to appeal the decision. More than 30 similar cases are pending in the EU. See "EU court rules for second time against Iran bank sanctions", Reuters, 6 February 2013.
[239] "In an economy of resistance the country continues to grow, but at the same time becomes less vulnerable. That is to say, our economy should not be seriously harmed or disrupted by our enemies' machinations ...". From "Supreme Leader's Speech to Researchers and Managers of Knowledge-Based Companies", Khemenei.ir (in Persian), 29 July 2012.
[240] According to Ayatollah Khamenei, "the thought that the cause of the arrogant front's enmity towards Iran is adopting certain stances or making certain decisions is wrong .... The cause of all these pressures is the Iranian nation's independent position and unwillingness to bow to the hegemonic system ... despite international sanctions, the Islamic Republic has become stronger .... During the last 33 years, Iran has been faced with a wide range of different political, security, military and economic sanctions, but the Iranian nation has defused these pressures and grown even more powerful through its resistance .... The Iranian nation will never surrender to pressures, and this has made the enemy furious", from "بیانات در دیدار شرکت‌کنندگان در ششمین همایش ملی نخبگان جوان" [Speech to the Sixth National Conference of Young Elite"], Khamenei.ir, 3 October 2012.
[241] Mehdi Mohammadi, "مقاومت محدود، مصونیت نامحدود" ["Limited Resistance, Unlimited Immunity"], *Kayhan*, 21 January 2012.

than by their sheer quantity and more visible and measurable economic consequences. Finally, as the West increases its leverage (not only through sanctions, but also through acts of sabotage), Tehran arguably feels it must do the same. It has few options: accelerating its nuclear program or resorting to its own forms of sabotage.[242]

B. *A Tortuous Untangling*

Both sides of the negotiating table face a dilemma. Each has invested considerable time and energy – not to mention reputation and prestige – often at the expense of other interests, in order to accumulate its respective assets. Iran's significant nuclear advances have come at huge and long-term economic costs and in hindsight would likely appear highly imprudent – even irresponsible – in the eyes of its public were they to be traded away without a concomitant improvement in ordinary citizens' living condition.[243] In other words, the longer the standoff endures, the higher the price Tehran likely is to demand to justify any consequential policy reversal. Sitting atop the Iranians' wish list most probably is the lifting of the sanctions that have proved particularly devastating, namely the financial restrictions and those on oil.[244]

The situation is equally complicated for the West. It has put together an impressive panoply of sanctions few would have thought conceivable not so long ago, because they were persuaded neither the U.S. nor, especially, the EU would take the risk of unnerving the oil market. Beginning to undo the sanctions regime would threaten to unravel the painstakingly constructed multilateral consensus; and it would face important political obstacles in Washington but also in European capitals. The U.S. and EU thus are unlikely to do so other than in response to meaningful, tangible Iranian concessions.

This raises an important issue regarding the use of sanctions as a tool of diplomacy aimed at policy change – as opposed to as a punitive instrument aimed at regime collapse. Such sanctions only are as effective as the prospect of relieving them in exchange for such shifts is real. In the Iranian case, the situation at best is murky in this regard. Although highly reluctant to acknowledge eagerness to see the sanctions lifted, Iranian officials routinely identify such a step as a condition sine qua non

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[242] An assessment of the pattern of mutual escalation during the past several years shows that, although they might not have prompted it to accelerate, sanctions have not deterred Tehran's nuclear advances. Nearly a month after the U.S. imposed unilateral sanctions on individuals and entities involved in the nuclear program on 28 June 2005, Iran notified the IAEA that it would resume its suspended uranium conversion activities. Then, almost two weeks after the Security Council adopted Resolution 1747 in March 2007, Iran announced it was installing 3,000 centrifuges in its nuclear facility in Natanz, reaching industrial-scale enrichment capacity. Shortly after the U.S. imposed sanctions on the central bank and the EU barred Iranian oil imports in early 2012, Tehran began enriching uranium at its underground Fordow facility. Most recently, Iran boasted that it had completed its centrifuge installation at Fordow following a new round of sanctions by Washington and Brussels in October 2012. At times, Iran has threatened to respond to punitive measures with more escalatory measures (such as enrichment to above 20 per cent or withdrawal from the NPT) but so far has shied away from doing so. Some analysts view the recent cyber-attack against Saudi Arabia's most important oil company as a possible warning shot from Tehran – an indication it could resort to different tactics should the economic warfare against it intensify. Crisis Group telephone interview, oil executive, Dubai, December 2012; Nicole Perlroth, "In cyberattack on Saudi firm, U.S. sees Iran firing back", *The New York Times*, 23 October 2012.
[243] Crisis Group interviews, Iranian official, December 2012; Hossein Mousavian, Washington, 29 August 2012.
[244] Ibid.

for any accord – and suspect the West is unlikely to take it.[245] Instead, they appear to fear a process in which their concessions are reciprocated by at best partial, reversible or even symbolic reprieve.[246] That, to date, no serious sanctions relief appears to have been offered has only bolstered such scepticism.[247]

Practical considerations also stand in the way. Even assuming Iranian willingness to compromise, the standard for lifting U.S. sanctions is high; the president can nullify his own executive orders but most have been codified by Congress, thereby limiting his room for manoeuvre.[248] He also can either exercise his waiver authority or order greater flexibility in enforcing the penalties.[249] But such short-term and easily reversible steps are unlikely to prompt meaningful Iranian concessions.[250]

What is more, not all U.S. sanctions are tied to the nuclear issue; many relate to Iran's foreign or domestic policies. As a result, without a fundamental reorientation of Iran's approach – highly improbable at this stage – a significant relaxation in sanctions is not in the cards. This is true of human rights-related sanctions; designations of persons for involvement in terrorism or pursuit of WMD;[251] the state of emergency regarding relations with Tehran; and Iran being on the list of states sponsoring terrorism.

The ambitious goals set out in the unilateral and multilateral sanctions thus appear in conflict with the more limited yet pressing goal of addressing the nuclear issue. The situation is compounded by at times discordant views between the executive and legislative branches, with the latter seemingly less interested in (or convinced of

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[245] For a review of Iran's most recent demands regarding sanctions, see Crisis Group Report, *The P5+1, Iran and the Perils of Nuclear Brinkmanship*, op. cit. More details emerged when Iran's mission to the UN published the five-point plan Tehran had proposed to the P5+1 during the June 2012 Moscow meeting. Sanctions relief was at the top of the list. Iran had proposed to cooperate with the IAEA on the issue of a possible military dimension of its nuclear program in return for repeal of all unilateral and multilateral sanctions. Subsequently, Iran offered to respond to the removal of UN sanctions by concessions on its 20 per cent uranium enrichment activities. See Barbara Slavin, "Iran seeks sustained dialogue", Al-Monitor.com, 4 July 2012.

[246] Crisis Group interview, Iranian official, December 2012. When, in October 2012, amid street protests triggered by the collapse of Iran's currency, U.S. Secretary of State Hillary Clinton said sanctions-induced economic problems could be "remedied in short order, if the Iranian government were willing to work with the international community in a sincere manner", Ayatollah Khamenei responded: "Now [Western countries] claim that if the Iranian nation desists from its nuclear energy, the sanctions will be lifted. They are telling a lie. Their decisions against the Iranian nation stem from their long-standing enmity". Quoted in "Iran atomic cooperation could spur fast sanctions relief: Clinton", Reuters, 3 October 2012; "West is foolish to celebrate Iran's rial crisis, Ayatollah Says", op. cit.

[247] See "History of Official Proposals on the Iranian Nuclear Issue", Arms Control Association, January 2013.

[248] See table in Appendix A below. For example, executive orders banning U.S. trade with Iran (EO 12957, EO 12959 and EO 13059) were codified by the Iran Freedom Support Act (IFSA) and CISADA. Similarly, sanctions on Iran's energy and petrochemical sector (EO 13590) and human rights violators (EO 13606) were subsequently legislated in the Iran Threat Reduction and Syria Human Rights Act (TRA).

[249] Crisis Group interviews, sanctions experts and former U.S. officials, Washington, December 2012.

[250] Crisis Group interviews, Iranian officials, October-December 2012.

[251] The U.S. employs an all-source evidentiary process for designations under different sanctions, and a delisting is conducted through the same process. Crisis Group interview, U.S. officials, Washington, December 2012. Designations under EO 13224 (involvement in terrorism), EO 13382 (WMD proliferators) and EO 13606 (human rights abusers) fall into this category.

the feasibility of) a diplomatic resolution, more eager to impose sanctions and less mindful of the views of Washington's allies. In Washington's presently highly politicised climate, Congress is unlikely to show the president much deference in this regard.

While EU sanctions are more elastic, lacking clear criteria for termination, their repeal nonetheless requires unanimity. This is not always a straight-forward enterprise.[252] Too, interaction among various U.S., EU and UN sanctions further complicates matters, as removing one piece might not be effective without removal of others. For instance, suspending restrictions on insuring Iranian oil shipments would necessitate modifications in both U.S. and EU legislation; what is more, such a change likely would have minimal practical effect because – even assuming elimination of transportation obstacles – Iran could not access oil revenues as long as financial restrictions remained in place. Likewise, any EU reversal would hinge on parallel steps in Washington to neutralise overlapping secondary sanctions. Then again, an EU concession risks being seen by Tehran as a tactical ploy if U.S. sanctions indefinitely remain in force.[253]

Finally, the effects of the sanctions in many cases arguably have acquired a life of their own, impervious at least in the short run to the persistence or lifting of the punitive measures themselves. This is because some trading and consumption patterns already have changed, after considerable investment of time and resources. Companies and countries that have shifted away from Iran are unlikely to rush back, at least short of assurances that the sanctions relief is long-term rather than temporary. A short-term suspension could provide a respite, but would have a limited impact, as uncertainty would make many loath to re-engage. In the oil sector in particular, reconfiguration of refineries that gradually have weaned themselves off Iranian crude, with its specific characteristics, would be both risky and economically unsound.[254]

All in all, the sanctions' multi-purpose and multi-layered nature has confused their strategic purpose, while constraining Washington's and Brussels' ability to respond to positive actions with requisite nimbleness.[255] Over time, as it simultaneously grew and ossified, the sanctions regime has become a less-than-optimal tool to advance negotiations in a diplomatic process where a scalpel, rather than a chainsaw, is required.[256]

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[252] Removing EU sanctions would entail difficult negotiations among the 27 member states; the subject is controversial enough that it is unlikely to even be broached in the absence of concrete Iranian concessions. Crisis Group interviews, EU official, Brussels, October 2012. Another official said, "the assumption that EU sanctions are the easiest to remove is a fallacy. It took great exertion to climb this mountain and would require the EU much effort to climb down it". Crisis Group interview, Brussels, June 2012.

[253] An Iranian official noted: "If we negotiate with the P5+1, we expect mutuality with the P5+1, not with the EU-3". Crisis Group telephone interview, Tehran, November 2012.

[254] Crisis Group interviews, energy experts, Washington, November-December 2012.

[255] Recent experience with other countries subjected to sanctions illustrates how multifaceted legislation and designations are hard to modify, even in the context of significant political change in the targeted country. See, eg, Crisis Group Asia Report N°231, *Myanmar: The Politics of Economic Reform*, 12 July 2012. In the Iranian case, both the Iran Sanctions Act (ISA) and the Comprehensive Iran Sanctions and Divestment Act (CISADA) are tied not only to Tehran's nuclear activities but also to its regional role and human rights record. Terminating them would require Iran to halt its nuclear and ballistic missile programs, take steps warranting removal from the list of state sponsors of terrorism, release all political prisoners and make progress toward the establishment of an independent judiciary.

[256] Asked about potential options for lifting some of the EU's restrictive measures, a senior European official said, "I have no idea, as I have never thought about it in the past". Crisis Group interview, Brussels, October 2012. Another European official acknowledged the complexity of the sanctions

V. Conclusion

A. *Rethinking Sanctions*

Many broad lessons can be learned from the international community's long experience with sanctioning Iran. First, and critically, are questions about the effectiveness of economic pressure as a tool of coercive diplomacy, ie, as a means of inducing specific policy changes. Although one cannot say with any certainty whether Iran would have gone farther in the absence of such pressure, one can confidently assert that the sanctions went hand in hand with advances in the nuclear program. Indeed, if the measure of that program's progress is the concern it inspires among outsiders, then clearly the sanctions have fallen far short of their purported objective.

Secondly, the case of Iran illustrates the risk that, precisely due to their inability to secure their primary goal, sanctions may turn into an end in and of themselves – or, stated differently, the measure of their success grows to be how many sanctions have been imposed and how much pain they inflict. That such pain does not translate into the desired policy change becomes, in this context, almost an afterthought. The pursuit of ever-escalating sanctions – in Iran, in Syria or elsewhere – often reflects competing pressures: the political imperative to do *something*; the understandable desire to avoid more perilous courses of action (notably, armed intervention); and the allure of an instrument yielding results that are easily measurable in terms of economic hardship. It is in some ways a path of least resistance, appealing both to hardliners who wish to exact a punishing price and to more moderate political actors who wish to avoid military action.

There are potential perverse incentives on both sides: on the part of the sanctioning party to intensify sanctions for the sake of intensifying them, but also on the part of the sanctioned party to bolster its own leverage in anticipation of future negotiations. In the Iranian case, this has meant an escalatory dynamic: more progress in Tehran's nuclear program mirroring more sanctions.

Another, larger point is this: that, as the reach and scope of sanctions expand, they not only miss their targets but play into the hands they intend to weaken. That those in power are better equipped to navigate the economic obstacle is nothing new, a fact of life witnessed in Iraq under Saddam as well as in Gaza under Hamas,[257] among many others. The economic distortions to which sanctions give rise can be manipulated so that rarefied goods are allocated to preferred constituencies, while those most prone to question their rulers are starved of resources. Again, this lesson can be witnessed today in Syria, with the advent of a war economy from which regime cronies (but also some rebel groups) can profit.[258]

Finally, there are the humanitarian consequences, which can often be brutal even as they lack the immediacy and drama of militarily-caused loss of life. Plus, a prolonged sanctions regime inevitably takes a serious social toll, making any future re-

regime: "It would not be an exaggeration to say no one is my country fully comprehends the sanctions regime". Crisis Group interview, Vienna, December 2012. Iranian officials appear equally uninformed about the sanctions intricacies and realistic options for lifting them. Crisis Group interview, current and former Iranian officials, March 2012-January 2013.

[257] See Crisis Group Middle East Report N°73, *Ruling Palestine I: Gaza Under Hamas*, 13 March 2008; Crisis Group Middle East Briefing N°24, *Round Two in Gaza*, 9 November 2008.

[258] See Crisis Group Middle East Report N°128, *Syria's Mutating Conflict*, 1 August 2012.

covery all the more difficult. Again, one need look no farther than the case of Iraq for illustration on both counts.

All this does not necessarily amount to an indictment of sanctions per se. But it does mean that they ought to be deployed far more prudently, thoughtfully and sparingly. Care also ought to be taken to continually assess the relation between the economic hardship that is inflicted and the policy goal that is pursued, as well as the practical effects on the ground of sanctions, whether they be dubbed "targeted", "smart" or otherwise. Western governments have discovered new means to squeeze other economies, notably through resort to financial penalties. But this should not be a reason for these to become weapons of first resort, without proper evaluation – and constant re-evaluation – of political efficacy, economic consequence and humanitarian impact.

B. *Sanctions: The Case of Iran*

But to return to Iran. A case study of both the economic success of sanctions and their political and humanitarian failings and drawbacks, it exhibits the various syndromes listed above: the tunnel vision that makes the weight of sanctions the measure of their success; the escalatory dynamic to which they contribute; the perverse incentives they unleash; the damaging social and humanitarian consequence to which they lead; and, of course, the risk that by placing all one's eggs in the sanctions basket, failure may appear to leave no other option but war. As much as any recent example, it cries out for a diligent examination of the impact of a large-scale and prolonged sanctions regime.[259]

It is, however, too late to reverse course; the question is how to move forward in light of the ongoing legacy of sanctions, of Iran's nuclear program and of mutual mistrust.

[259] A bipartisan group of U.S. national security experts and former officials recommended: "[The] United States might be better able to gauge the effectiveness of recent sanctions if the objectives that are most relevant and pressing today could be disentangled from other objectives that have been linked with sanctions. Or, to put this differently: If resolving the nuclear issue is now the most important objective of the sanctions regime, then sanctions strategies – and the negotiating strategy associated with sanctions – should be assessed in terms of their effectiveness in achieving that objective". See "Weighing Costs and Benefits of International Sanctions Against Iran", The Iran Project, December 2012. At present, multiple U.S. government agencies evaluate the effects of sanctions on Iran's energy sector, economy, politics and society. Yet, given that the U.S. lacks diplomatic representation in Iran, these assessments at best are imperfect. The UN Panel of Experts also publishes an annual report detailing the effects of sanctions and Iran's infringements. Most of its members represent sanctioning states, raising questions about potential bias and diminishing the weight of its recommendations. Crisis Group interview, sanctions expert, Brussels, September 2012. Finally, the EU – as a community, not individual member states – lacks any mechanism for a clear and transparent evaluation of the impact of sanctions. Although unilateral sanctions are chiefly responsible for humanitarian harm, disaggregating their impact from that caused by international sanctions is near impossible. The UN Security Council could take it upon itself to monitor, report on and make recommendations regarding adverse humanitarian consequences of sanctions in Iran, based on the methodology outlined in the UN Sanctions Assessment Handbook, which focuses on the 4+4 human security subject areas (health, food and nutrition, water and sanitation, education, governance, economic status, physical environment, and demography). The handbook is available at http://ochanet.unocha.org/p/Documents/IASCSanctionsHB2004.pdf. Also see Letter by Five Permanent Members of the Security Council on Humanitarian Impact of Sanctions, S/1995/300, 13 April 1995.

Failure to date to change Iran's nuclear calculus chiefly by sanctions and other coercive tools has given rise to various conclusions. Some argue that the answer to the inability of pressure to produce results should be more pressure, that the economic consequences need to be felt more starkly for the regime to feel compelled to adjust its approach. For those convinced of the regime's determination to acquire a nuclear weapon at all costs, it stands to reason that nothing – perhaps other than an imminent threat to its survival – can cause it to shift course.[260] Finally, many who believe a deal possible contend that sanctions are insufficient, even counter-productive, insofar as they essentially persuade Iran's leaders that the goal is regime change and thus discourage any compromise that risks being interpreted as a sign of weakness. Some go so far as to contend that heightened coercive measures are precisely what might push Tehran to cross the military threshold.[261] They fault the U.S. in particular for not taking the engagement track of the two-track policy as seriously as it did the pressure track.[262]

As Crisis Group long has argued, and without reaching a definitive conclusion as to the Islamic Republic's intent, there is good reason to be concerned about possible military implications of Iran's nuclear program.[263] But there is equally good reason not only to avoid an armed attack against Iran of unpredictable and potentially wide-scale consequence, but also to question whether sanctions are the proper remedy – at least as presently construed. The question today is whether the P5+1 can offer a combination of preliminary sanctions relief and political incentives capable of prompting Iran to take its own initial steps on the nuclear file sufficient both to reassure the West and set in motion a more ambitious negotiation process – and whether all this can be done before the U.S. or Israel deems it too late.[264]

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[260] "Iran will stop only when the cost of moving towards nuclear weapons will be higher than the cost of not doing so. Only a threat to the existence of the regime can achieve that". Crisis Group interview, Israeli defence official, Jerusalem, December 2012.

[261] A former Iranian official said, "it defies logic that Iran, an NPT-signatory with no nuclear weapons, is under more sanctions than North Korea, which has developed several nuclear devices and withdrew from the NPT. I think the West is pushing Iran in the wrong direction". Crisis Group interview, Hossein Mousavian, Princeton, 6 January 2013.

[262] Vali Nasr, a former adviser to the U.S. State Department, argues that U.S. acts of sabotage and economic pressure "[make] attaining nuclear weapons of critical importance to the clerics. Without such weapons, Iran could face the Libya scenario: economic pressure causing political unrest that invites intervention by foreign powers that feel safe enough to interfere in the affairs of a non-nuclear-armed state. The more sanctions threaten Iran's internal stability, the more likely the ruling regime will be to pursue nuclear deterrence and to confront the West to win the time Iran needs to reach that goal". "Hard-line US Policy tips Iran toward belligerence", Bloomberg, 5 January 2012.

[263] See previous reporting, in particular, Crisis Group Reports, *In Heavy Waters*; *Iran: Is There a Way Out of the Nuclear Impasse?*; and *Dealing with Iran's Nuclear Program*, all op. cit.

[264] By completing the underground facility at Fordow, Iran arguably already crossed an Israeli redline – though the shifting nature of Israeli positions makes this difficult to ascertain. More recently, Prime Minister Benjamin Netanyahu asserted that his country's red line was the point at which Iran's stockpile of 20 per cent enriched uranium would be sufficient for one nuclear bomb. He predicted that, should nothing change, Iran would reach that point by spring or summer 2013. See Jeffrey Heller, "Netanyahu draws 'red line' on Iran's nuclear program", Reuters, 27 September 2012. For a review of Israel's past red lines on Iran's nuclear program, see Graham Allison, "Red Lines in the Sand", *Foreign Policy* (online), 11 October 2012; for an Iranian perspective on Fordow, see "Fordow's full operation to immunise Iran's peaceful nuclear program", Fars News Agency, 21 November 2012. Concerns now appear to be focused on assessing when Iran will have entered a "zone of invisibility" – the point at which it could produce sufficient weapon-grade enriched uranium for one or more nuclear warheads without detection by outsiders, or quickly enough so that detection

An honest answer would have to be: we do not know. Tehran may have decided long ago that a nuclear weapon is the only effective deterrent to regime change; it may have decided that more recently in response to perceived Western belligerence; or it may not have decided it at all. What is clear is that all conceivable alternatives appear worse than a negotiated agreement; that, so far, a meaningful offer has yet to be presented to Iran (just as Iran so far has failed to put forward a meaningful concession); and that it is long past time for such an offer to be made. A grand bargain that would seek to put to rest years of accumulated enmity would be preferable, but it is presently out of reach, given how deeply entrenched both the nuclear program and the sanctions regime have become, as well as the high level of mutual mistrust; placating the West's core concerns and unravelling the intricate web of sanctions simply cannot be done in one go.

Instead, the immediate objective should be a gradual, incremental approach that sets a more constructive process in motion; puts more time on the proverbial nuclear clock; and allows both sides to retain sufficient leverage to guard against the other's potential reneging.[265] More than a decade after the advent of the' nuclear crisis, any successful diplomatic process will require time and patience. Both the nuclear program and the sanctions regime are multi-layered, so their respective reversals are bound to be slow and, for the time being, incomplete.[266]

The challenge is to come up with a P5+1 package of meaningful, albeit realistic sanctions relief to match a parallel Iranian package of meaningful, albeit realistic nuclear concessions. Meaningful sanctions relief, from an Iranian standpoint, signifies reversal of some measures that have significantly affected its economic well-being;[267] realistic signifies that they can be lifted, waived or suspended given legal and political constraints in the sanctioning entities.[268] In mirror image, Iran's nuclear concessions should provide some reassurance to the P5+1 as to its ability to break-out even as

would be futile. Most recent estimates put that point sometime in mid-2014. See, eg, "U.S. Nonproliferation Strategy for the Changing Middle East", Institute for Science and International Security, 14 January 2013.

[265] A non-proliferation expert noted: "Just as the U.S. would want leverage to make sure Iran keeps its commitments, so too will they need leverage to ensure the U.S. keeps whatever commitments it makes. In fact, Washington should want the Iranians to keep leverage because it would actually increase the probability of their living up to any agreement. If the U.S. demands that Iran entirely give up its enrichment of uranium, they are bound to cheat on any nuclear agreement, like the North Koreans did". Crisis Group interview, George Perkovich, director, Nuclear Policy Program, Carnegie Endowment for International Peace, Washington, 1 June 2012.

[266] A U.S. expert wrote: "It is unrealistic to expect a state to reach an overnight realisation that nuclear weapons are not in its national interest. Instead, any such decision can only emerge in the aftermath of sustained engagement demonstrating the trade-offs inherent in defying the will of the international community, a point demonstrated by the years of negotiation preceding Libya's decision and … the agreement forged in the Six-party Talks on North Korea. In fact, demanding a permanent strategic decision may inadvertently discourage rogue regimes from taking intermediate steps that make the world more secure, including "half-loaf" compromises that fail to resolve a state's underlying proliferation desires but effectively constrain its arsenal for a period of time. Although messy, these steps can buy the necessary time to allow a permanent solution to emerge while securing our national interests in the interim". Jofi Joseph, "Strategic Mistake", *Democracy Journal*, issue 4, spring 2007.

[267] Appendix A below identifies those sanctions whose lifting, modification or suspension would most benefit Iran.

[268] The degree of difficulty in lifting, amending or suspending sanctions is also identified in Appendix A below.

they fall slightly short of the demands currently made – the "stop, ship and shut" package, pursuant to which Iran would stop its 20 per cent uranium enrichment; ship out its existing stockpile of uranium enriched to that level; and shut down its underground Fordow facility.[269]

In June 2012, Crisis Group proposed just such a calibrated approach. By and large it remains relevant, although intervening events (the completion of Fordow; additional sanctions; and Iran's conversion of some of its 20 per cent uranium hexafluoride into pellets of uranium oxide to be used for nuclear fuel fabrication) necessitate some tweaking.[270]

As to the format of talks: If anything, the need for a more sustained form of engagement has become even more evident. Reaching agreement on a detailed package likely will require a lengthy process for which sporadic, high-level diplomatic encounters such as the scheduled 26 February talks at Almaty, are unsuitable. Given the level of technical complexity, expert-level meetings will be required to reach any agreement.[271] Iran and the P5+1 might establish a Vienna- or Istanbul-based contact group aimed at regular interaction far from the media spotlight. Direct bilateral talks between Iran and the U.S. likewise ought to be seriously considered, an issue that has been raised repeatedly by Washington, but not always in contexts likely to encourage a positive response from Tehran.[272]

As to the immediate issue of 20 per cent enrichment: Iran should be prepared to both suspend its 20 per cent enrichment for a period of 180 days and convert its entire stockpile of 20 per cent enriched uranium to fuel rods.[273] This would effectively restrict operations at Fordow[274] and address the most urgent proliferation

[269] See Crisis Group Briefing, *The P5+1, Iran and the Perils of Nuclear Brinkmanship*, op. cit.
[270] Ibid.
[271] Members of both the Iranian and U.S. negotiating teams confirm that the technical meetings conducted in July 2012 in Istanbul have been among their most productive and useful discussions to date. Crisis Group interviews, Iranian and U.S. officials, July 2012, February 2013.
[272] In February 2013, for example, Vice President Joe Biden reasserted U.S. willingness to engage in such talks in February 2013, assuming Iran's leaders were serious about negotiations. The Iranian foreign minister welcomed the idea, calling it "a step forward". Coincidentally, a provision of the Iran Threat Reduction and Syria Human Rights Act went into effect a few days later, depriving Iran of hard currency from its oil sales – a development highlighting difficulties in fine-tuning a policy of pressure and of engagement. The next day, Ayatollah Khamenei dismissed the opening, saying, "The Iranian nation will not negotiate under pressure .... The U.S. is pointing a gun at Iran and wants us to talk to them. The Iranian nation will not be intimidated by these actions". See David Sanger, "Supreme Leader of Iran rejects direct talks with U.S.", *The New York Times*, 7 February 2013.
[273] Uranium oxide raises fewer proliferation concerns, as it would have to first be converted back to a gaseous form before enrichment to weapons-grade levels, a lengthy process easily detectable by IAEA inspections. Since June 2012, when Crisis Group first proposed this measure, Iran has converted nearly 40 per cent of its 20 per cent stockpile to uranium oxide. Israeli officials suggested that the move had mitigated some of their concerns over a rapid dash towards weaponisation. See Rick Gladstone, "Israeli defense chief says Iran postponed nuclear ambitions", *The New York Times*, 30 October 2012. In June, Crisis Group wrote: "This would be a win-win situation, insofar as it would significantly reduce proliferation risks … while allowing Iran to maintain its stockpile in the country". *The P5+1, Iran and the Perils of Nuclear Brinkmanship*, op. cit.
[274] Currently Iran only refines uranium to 20 per cent level at Fordow. However, according to the Design Information Questionnaire (DIQ) of the facility, its intended use is for enrichment at both 5 and 20 per cent levels. See "Implementation of safeguards in Iran: GOV/2013/6", Director General of the IAEA, 6 February 2013.

concern, thus meriting a reciprocal step of commensurate value. Simultaneously, the P5+1 would:

(1) provide medical isotopes needed for the treatment of some 850,000 cancer patients;
(2) freeze any new sanctions;
(3) amend, waive or suspend some sanctions for the same 180-day period. For example, both the U.S. and EU could suspend their ban on the sale and transfer of precious metals (such as gold) as well as semi-finished metals (such as steel) to Iran.[275] Alternatively, or additionally, the U.S. could waive sanctions on the repatriation of Iran's revenues from oil sales to its remaining customers, and the EU could suspend the ban on all transactions between European and Iranian banks;[276] and
(4) agree to release some of Iran's frozen assets.[277]

Such an initial tradeoff would reflect willingness to resolve the impasse; blunt the proposition that sanctions are untouchable; and widen the time horizon for resolving more contentious issues. If, after six months, negotiations are advancing in the right directions, both sides could renew their suspensions for an additional 180 days.

As to the issue of Fordow: In June, Crisis Group noted that it was unrealistic to expect Iran to shut down its Fordow enrichment facility; that assessment is all the more true now that the facility has been completed. Still, Iran should accept to maintain the status quo, thereby refraining from installing any advanced centrifuges – an issue of considerable concern to the West and Israel. (In Natanz, Tehran could continue developing and modernising its centrifuges, but only upon reaching agreement with the IAEA to upgrade the facility's safeguard measures as necessary.)[278]

[275] This would allow Iran to barter its oil sales for gold and obtain the steel and aluminium necessary for the effective functioning of its industrial sector. President Obama could invoke his authority to waive provision 1245 of the Iran Freedom and Counter Proliferation Act of 2012 to allow the sale, supply and transfer of such metals for a renewable period of 180 days based on U.S. national security considerations. Before the February 2013 resumption of the P5+1 and Iran negotiations in Kazakhstan, media reports indicated that the P5+1 would offer to ease sanctions barring trade in gold and other precious metals in return for Iran shutting down Fordow. See Arshad Mohammed, "Big powers to offer easing gold sanctions at Iran nuclear talks", Reuters, 15 February 2013. Iranian officials immediately dismissed the suggestion; a foreign ministry spokesperson said, "lately they [the West] have said 'Shut down Fordow, stop (uranium) enrichment, we will allow gold transactions', …. They want to take away the rights of a nation in exchange for allowing trade in gold". Quoted in Reuters, 18 February 2013.

[276] Such a measure would allow Iran to repatriate the hard currency necessary for sustaining the rial. Obama could invoke his authority to waive the prohibition on repatriating Iran's oil receipts (section 504 of the Iran Threat Reduction and Syria Human Rights Act). A unanimous EU decision would be required to modify for similar durations relevant provisions in Council Decision 2010/413 / CFSP as amended by Council Decision 2012/635/CFSP and Council Regulation 1263/2012.

[277] Implementing a decision to release part of Iran's frozen assets should be relatively straightforward, as it would require executive decisions by the U.S. president and the EU Council.

[278] Most of Iran's enrichment is done with antiquated IR-1 centrifuges that regularly break down. Tehran has spent at least seven years seeking to develop more efficient machines. In February 2013, it informed the IAEA of its intention to install 3,000 of the far more powerful and advanced IR-2m centrifuges in Natanz. As of this writing, Iran had installed 180 and 162 of them, respectively, in its fuel enrichment and pilot plants in Natanz. The facility also contained several other complete or partially-complete cascades of other more advanced models. The U.S. State Department called the move "yet another provocative step", while Israeli Prime Minister Benjamin Netanyahu's office said

Other steps previously proposed – agreement by Iran to use the Fordow centre exclusively for research and development purposes as well as to upgrade the IAEA's safeguards agreement for Fordow to allow in-house resident inspectors or installation of live-stream remote camera surveillance – also should be taken. In return the U.S. and EU could suspend their sanctions on Iran's petrochemical sector[279] or halt pressure on Iran's remaining oil customers to significantly reduce their purchases of Iranian petroleum.[280]

As to the humanitarian issues: As seen, and although the sanctions formally exempt medicine in particular, their chilling and other unintended effects in fact have contributed to worsening the situation.[281] The U.S. Treasury and the EU Council. should provide clear guidelines and encourage third-party banks to conduct authorised humanitarian transactions.[282] But such a step would only partially resolve the problem, as Iran's limited access to hard currency and challenges in obtaining insurance and shipping services still likely would significantly hamper the purchase of foreign medicine.

Given the narrowness of the problem – shortages affect approximately 50 pharmaceutical products – one possible solution would be to delegate such specialised medicine procurement to an independent intermediary, such as an international agency.[283]

that this "proves Iran continues to advance swiftly toward the red line". *The New York Times*, 22 February 2013. Iran is unlikely to agree to abandon such latter-generation centrifuges; from a non-proliferation perspective, having them at Natanz is less worrying if their numbers are limited and their functioning is accompanied by stringent monitoring and enhanced safeguards. Fordow is a different matter given its greater invulnerability to any military strike in case of a rapid dash towards weaponisation.

[279] Relaxing sanctions on Iran's petrochemical industry – an important source of revenue – would require the U.S. administration to waive relevant provisions under Executive Order 13622 and section 201 of the Iran Threat Reduction and Syria Human Rights Act of 2012. For its part, the EU council would need to modify provisions under Council Decision 2012/35/CFSP and the related Council Regulations.

[280] To allow Iran to maintain current levels of oil export, President Obama could invoke the national security-based waiver pursuant to section 1245 of the National Defense Authorization Act of 2012, which authorises sanctions exemptions for Iranian oil customers for renewable periods of 120 days.

[281] U.S. officials point out that they have been careful to ensure that medical exports to Iran are not disrupted and blame Tehran for mismanaging and exploiting the issue for propaganda purposes. Crisis Group interview, senior U.S. official, Washington, February 2013. That said, sanctions have made international banks reluctant to conduct any transactions – including those related to humanitarian trade – with Iran and led to a scarcity of hard currency needed for trade with European and American manufacturers. See Siamak Namazi, "Sanctions and Medical Supply Shortages in Iran", Viewpoints no.20, Woodrow Wilson Center for Scholars, February 2013. U.S. Treasury officials are loath to create a "whitelist" of reputable financial institutions to conduct transactions related to medical purchases, as such action in practice would allow a few banks to monopolise a relatively lucrative commercial activity. They also are guided by the risk that such a mechanism might be used for banned activities. Crisis Group interviews, Washington, December 2012.

[282] Another solution would be for the U.S. Treasury and EU officials to issue general or specific licences authorising third-country financial institutions to process payments for authorised humanitarian products involving Iranian banks currently prohibited from participating in such transactions. Crisis Group interview, OFAC practitioner, Washington, 19 February 2013.

[283] Fatemeh Hashemi, head of Iran's Foundation for Special Diseases, suggested creating such a channel through the Food and Agriculture Organization (FAO) and Iran's Agricultural Bank, which is not subject to international sanctions. Crisis Group telephone interviews, Fatemeh Hashemi;

For its part, the Iranian government should streamline its currency allocation, licensing and customs procedures for medical imports.

Further down the road, a more detailed roadmap of reciprocal concessions, in the context of a longer-term agreement, could include the following:

(1) Iran's agreement not to surpass a mutually acceptable quantity of stockpiled 5 per cent enriched uranium, with any amount in excess to be converted into fuel rods; in return, the P5+1 would provide Tehran with modern and safe nuclear fuel manufacturing technology,[284] while rolling back restrictions affecting Iran's financial system;[285]

(2) In return for Iran's agreement to ratify and implement the IAEA's Additional Protocol and Code 3.1 (pursuant to which Tehran would be required to inform the agency of any new nuclear facility at the time a decision to build one is taken) and establish an enhanced safeguards monitoring system for its nuclear facilities, the U.S. and EU would remove or suspend oil sanctions, allowing Iran to increase its petroleum exports.[286] This step would require substantial coordination between Washington and Brussels, as well as with oil-producing countries such as Saudi Arabia, which likely would need to cut back production to make space for Iranian crude oil.[287]

To further facilitate progress, both sides from the outset should clarify the broad principles governing the endgame: recognition in principle by the P5+1 of Iran's right to enrich uranium for peaceful purposes on its soil on the one hand;[288] acceptance by

FAO representative in Iran, Tehran, 6 December 2012. However, the task arguably would be more appropriate for an international agency such as the World Health Organization.

[284] Technology related to light-water civilian nuclear reactors are exempt from UN sanctions.

[285] Possible measures include reversing the determination that Iran is a jurisdiction of primary money-laundering concern, delisting specific Iranian banks from the list of sanctioned entities (thus allowing them to use SWIFT) and removing the ban on providing financial messaging services to Iran.

[286] To resume importing Iranian oil, the EU Council would have to lift or suspend sanctions related to crude imports as well as those affecting the provision of shipment insurance and reinsurance. At the same time, the U.S. president would have to revoke Executive Order 13622 and waive for a renewable period of 120 days sanctions against countries that resume or increase their oil imports from Iran. The president also would have to waive sanctions related to provision of insurance and re-insurance for shipments of Iran's energy products. Finally, both the EU and U.S. would need to delist the National Iranian Oil Company and the National Iranian Tanker Company.

[287] Crisis Group interview, U.S. official, Washington, November 2012. This is no easy matter. Indeed, any short-term suspension would be practically futile, as the uncertainty would render reconfiguration of refineries, which already have weaned themselves off of the specific type of Iranian crude, risky and economically unsound. Moreover, all aspects relevant to Iran's oil sales, including shipping, insurance and financial transactions, would need to be addressed simultaneously. As the oil market is likely to be saturated in 2013, the prospects of Iranian oil finding customers would be difficult in the absence of cooperation from other OPEC members.

[288] As Crisis Group wrote: "While de jure recognition of Iran's nuclear rights under the NPT is not realistic before the IAEA attests to the peaceful nature of its nuclear program, the P5+1 should clearly convey to Tehran that – once that condition has been met – it will be entitled to enrich on its soil under IAEA supervision. Until that stage is reached, the P5+1 ought to offer de facto recognition of that right, albeit within reasonable restrictions including, inter alia, capping the level of purity (at 5 per cent), limiting the number of facilities to Natanz and Fordow, freezing the number or type of centrifuges they contain for an agreed period of time and instituting a rigorous monitoring system by UN nuclear inspectors". *The P5+1, Iran and the Perils of Nuclear Brinkmanship*, op. cit.

Iran of legitimate international concerns regarding its nuclear program and agreement to steer clear of acquiring short-term breakout capability. Both sides have signalled, in theory at least, some willingness to move in this direction. Iran's foreign minister said:

> We are ready to recognise the concerns over the peaceful nature of our nuclear program. We welcome any transparency measure, be it the Additional Protocol or Code 3.1 that could reassure the world. These measures are all in line with the Supreme Leader's *fatwa* (judicial opinion) against nuclear weapons, which we are willing to register at the UN as a legally binding document.[289]

Likewise, in March 2011, former U.S. Secretary of State Hillary Clinton said, "it has been our position that under very strict conditions Iran would, sometime in the future, having responded to the international community's concerns and irreversibly shut down its nuclear weapons program, have such a right [to enrich] under IAEA inspections".[290]

In parallel, Iran and the IAEA should agree on a structured framework to resolve the agency's outstanding thirteen questions regarding possible military dimensions of Iran's nuclear program.[291] The P5+1 and Iran should agree on a formula that links incremental lifting of other nuclear-related sanctions with resolution of specific issues between Iran and the IAEA. Once Tehran has answered questions to the IAEA's satisfaction, the P5 should submit and sponsor a new resolution in the Security Council removing existing UN sanctions and returning Iran's file to the UN nuclear agency.

Regardless of the precise sequence of negotiated steps, time is of the essence. With Iran's presidential poll scheduled for June 2013, some have argued that Tehran will do nothing meaningful until then and, therefore, that a serious process will have to await.[292] Perhaps. But reading the tea leaves of Iranian politics is an inexact science at best and one at which Western policymakers have not shown themselves to be particularly adept. An interim nuclear deal could prove contentious domestically and thus interfere with the elections; conversely, it might prove popular and thus facilitate them. The same will hold true with a newly-installed president, who might be eager for an achievement, or loath to invite controversy.

In any event, key decisions in this area, virtually all agree, rest with the Supreme Leader, not with whomever inherits the presidential mantle. The road ahead will be long and tortuous no matter what. The sooner it is begun, the better.

Washington/Brussels, 25 February 2013

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[289] Crisis Group interview, Ali Akbar Salehi, New York, 25 September 2012.
[290] See Peter Crail, "U.S. position on Iran enrichment: more public recognition than policy shift", Arms Control Now, 30 April 2012.
[291] Since the IAEA published details of outstanding issues with Iran in November 2011, Iranian and agency officials have met nine times to hammer out an agreement over a framework pursuant to which Tehran would provide answers. So far, progress has been at a crawl. See Jonathan Tirone and Ladane Nasseri, "Iran, IAEA fail to agree on deal; no new date set for talk", Bloomberg, 14 February 2013.
[292] Crisis Group interview, U.S. analyst, Washington, February 2013.

Appendix A: Major Unilateral, Multilateral and International Sanctions Imposed on Iran

1. Key

Ease of Repealing	
1	**The executive branch can unilaterally amend or repeal the measure.** U.S. executive orders not tied to congressional legislation.
2	**Multilateral consensus is required for modifying or repealing the measure.** EU restrictive measures requiring consensus by all member states.
3	**Amending or repealing sanctions adopted by UN Security Council resolutions require a new resolution.**
4	**Requires legislative action, often including specific criteria for termination.** U.S. acts of Congress or executive orders tied to acts of Congress.

Ease of Suspending	
1	**The executive branch can unilaterally and indefinitely suspend the measure.** U.S. executive orders not tied to congressional legislation.
2	**The executive branch can suspend the measure, but must report/explain to Congress. Time-restricted waivers are often renewable. Also, cases where suspension requires a unanimous decision by a multilateral body.** U.S. acts of Congress with discretion on implementation and renewable waiver authority. EU restrictive measures.
3	**Suspending sanctions adopted by UN Security Council resolutions require a new resolution.**
4	**No waiver authority.** Some U.S. acts of Congress.

Economic Impact			
H	High	**L**	Low

Acronyms

CFSP	Common Foreign and Security Policy
CISADA	Comprehensive Iran Sanctions, Accountability, and Divestment Act
EO	Executive Order
IEEPA	International Emergency Economic Powers Act
IFCPA	Iran Freedom and Counter-Proliferation Act of 2012
IFSA	Iran Freedom Support Act
INKSNA	Iran, North Korea, and Syria Nonproliferation Act
ISA	Iran Sanctions Act
ITRSHRA or **TRA**	Iran Threat Reduction and Syria Human Rights Act
NDAA	National Defense Authorization Act
NEA	National Emergencies Act
NPT	Non-Proliferation Treaty
TEC	Treaty establishing the European Community
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
UNSCR	United Nations Security Council Resolution

2. U.S. Executive Orders

U.S. Executive Orders	Year	Trigger				Targets								Status	Economic Impact	Ease of Repealing	Ease of Suspending
		Nonproliferation	Terrorism	Human Rights	Other	Arms	Nuclear/ Missile	Financial	Energy	Travel bans	Asset Freeze	Trade ban*	Other				
EO 12170	1979				X						X			Modified	L	1	1
EO 12205	1980				X			X				X		Revoked	N/A	N/A	N/A
EO 12211	1980				X			X		X		X		Revoked	N/A	N/A	N/A
EO 12613	1987		X		X				X			X		Revoked	N/A	N/A	N/A
EO 12957	1995				X				X					Codified	H	4	4
EO 12959	1995				X							X		Codified	H	4	4
EO 13059	1997				X							X		Codified	H	4	4
EO 13224	2001		X					X			X				L	1	1
EO 13382	2005	X					X	X			X				L	1	1
EO 13553	2010			X						X	X				L	1	1
EO 13572	2011			X							X				L	1	1
EO 13574	2011				X			X			X				H	4	4
EO 13590	2011	X						X	X		X			Codified	H	4	4
EO13599	2012				X			X			X				H	1	1
EO 13606	2012			X						X	X		X	Codified	L	4	4
EO 13608	2012				X			X		X	X				L	1	1
EO 13622	2012				X			X	X		X				H	1	1
EO 13628	2012	X	X	X		X	X	X	X	X	X	X			H	4	4

* Trade ban applies to both partial and total bans.

3. U.S. Acts of Congress

		Trigger				Targets											
U.S. Congressional Legislation	Year	Nonpro liferation	Terrorism	Human Rights	Other	Arms	Nuclear/ Missile	Financial	Energy	Travel bans	Asset Freeze	Trade ban*	Other	Status	Economic Impact	Ease of Repealing	Ease of Suspending
National Defense Authorization Act of 1993	1992	X				X	X								L	4	2
Iran Sanctions Act (ISA)	1996	X	X						X					Amended	H	4	2
Iran Nonproliferation Act	2000	X				X	X				X			Renamed INKSNA	L	4	4
Iran Freedom Support Act (IFSA)	2006	X	X	X		X	X	X	X					Replaced	N/A	N/A	N/A
Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA)	2010	X	X	X	X	X	X	X	X	X	X	X		Amended	H	4	2
Iran-Syria-North Korea Nonproliferation Act (INKSNA)	2011	X				X	X				X				L	4	4
Section 311 of the USA Patriot Act	2011	X	X		X			X							H	4	1
National Defense Authorization Act of 2012, Sec 1245	2011	X	X		X			X	X		X			Amended	H	4	2
Iran Threat Reduction and Syrian Human Rights Act of 2012 (ITRSHRA OT TRA)	2012	X	X	X				X	X	X	X	X	X		H	4	2
National Defense Authorization Act of 2013, Subtitle D	2012	X	X	X				X	X		X	X	X		H	4	2

* Trade ban applies to both partial and total bans.

4. EU Restrictive Measures

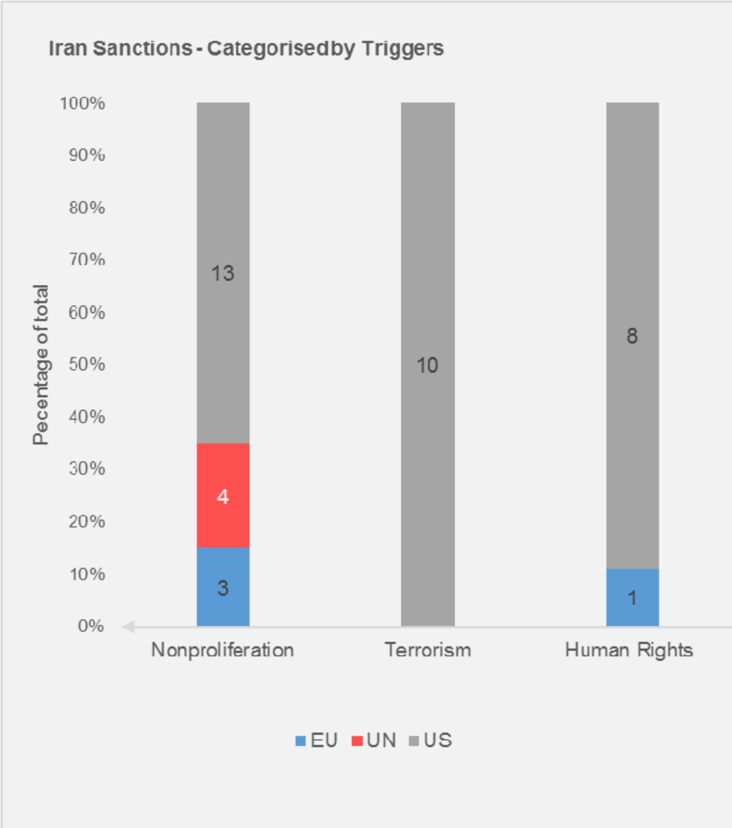
EU Restrictive Measures	Year	Trigger				Targets								Status	Economic Impact	Ease of Repealing	Ease of Suspending
		Nonproliferation	Terrorism	Human Rights	Other	Arms	Nuclear/ Missile	Financial	Energy	Travel bans	Asset Freeze	Trade ban*	Other				
Council Common Position 2007/140/CFSP, Council Regulation 423/2007	2007	X				X	X	X		X	X			Replaced	N/A	N/A	N/A
Council Decision 2010/413/CFSP, Council Regulation 961/2010	2010	X				X	X	X	X	X	X	X	X	Amended	H	2	2
Council Decision 2011/235/CFSP, Council Regulation 359/2011	2011			X						X	X	X		Amended	L	2	2
Council Decision 2012/35/CFSP, amending 2010/413/CFSP, Council Regulation 267/2012	2012	X				X	X	X		X	X	X		Amended	H	2	2

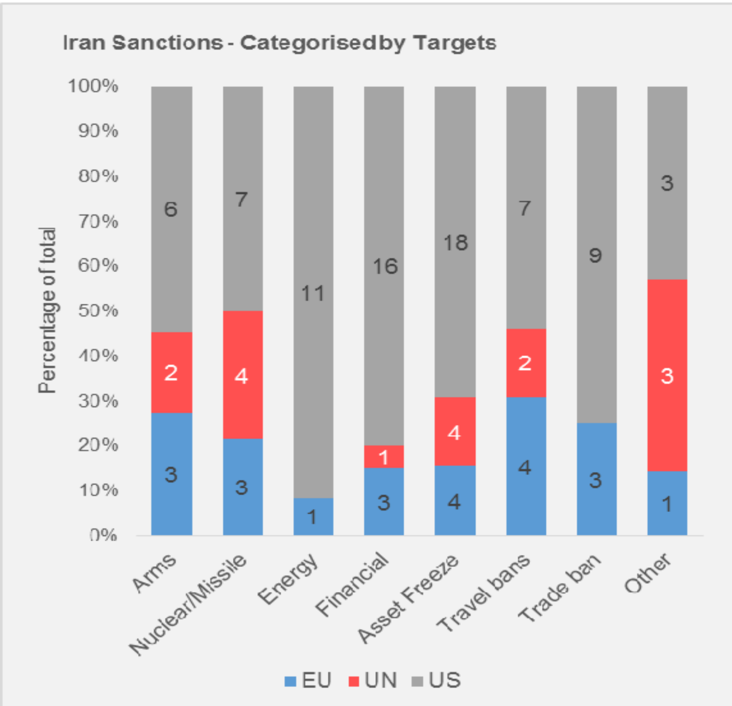
5. UN Security Council Resolutions

UN Security Council Resolutions	Year	Trigger				Targets								Status	Economic Impact	Ease of Repealing	Ease of Suspending
		Nonproliferation	Terrorism	Human Rights	Other	Arms	Nuclear/ Missile	Financial	Energy	Travel bans	Asset Freeze	Trade ban*	Other				
United Nations Security Council Resolution 1737	2006	X					X				X		X		L	3	3
United Nations Security Council Resolution 1747	2007	X				X	X				X				L	3	3
United Nations Security Council Resolution 1803	2008	X					X			X	X		X		L	3	3
United Nations Security Council Resolution 1929	2010	X				X	X	X		X	X		X		H	3	3

* Trade ban applies to both partial and total bans.

Appendix B: Iran Sanctions Based on Triggers and Targets





Appendix C: About the International Crisis Group

The International Crisis Group (Crisis Group) is an independent, non-profit, non-governmental organisation, with some 150 staff members on five continents, working through field-based analysis and high-level advocacy to prevent and resolve deadly conflict.

Crisis Group's approach is grounded in field research. Teams of political analysts are located within or close by countries at risk of outbreak, escalation or recurrence of violent conflict. Based on information and assessments from the field, it produces analytical reports containing practical recommendations targeted at key international decision-takers. Crisis Group also publishes *CrisisWatch*, a twelve-page monthly bulletin, providing a succinct regular update on the state of play in all the most significant situations of conflict or potential conflict around the world.

Crisis Group's reports and briefing papers are distributed widely by email and made available simultaneously on the website, www.crisisgroup.org. Crisis Group works closely with governments and those who influence them, including the media, to highlight its crisis analyses and to generate support for its policy prescriptions.

The Crisis Group Board – which includes prominent figures from the fields of politics, diplomacy, business and the media – is directly involved in helping to bring the reports and recommendations to the attention of senior policy-makers around the world. Crisis Group is chaired by former U.S. Undersecretary of State and Ambassador Thomas Pickering. Its President and Chief Executive since July 2009 has been Louise Arbour, former UN High Commissioner for Human Rights and Chief Prosecutor for the International Criminal Tribunals for the former Yugoslavia and for Rwanda.

Crisis Group's international headquarters is in Brussels, and the organisation has offices or representation in 34 locations: Abuja, Bangkok, Beijing, Beirut, Bishkek, Bogotá, Bujumbura, Cairo, Dakar, Damascus, Dubai, Gaza, Guatemala City, Islamabad, Istanbul, Jakarta, Jerusalem, Johannesburg, Kabul, Kathmandu, London, Moscow, Nairobi, New York, Pristina, Rabat, Sanaa, Sarajevo, Seoul, Tbilisi, Tripoli, Tunis and Washington DC. Crisis Group currently covers some 70 areas of actual or potential conflict across four continents. In Africa, this includes, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Côte d'Ivoire, Democratic Republic of the Congo, Eritrea, Ethiopia, Guinea, Guinea-Bissau, Kenya, Liberia, Madagascar, Nigeria, Sierra Leone, Somalia, South Sudan, Sudan, Uganda and Zimbabwe; in Asia, Afghanistan, Burma/Myanmar, Indonesia, Kashmir, Kazakhstan, Kyrgyzstan, Malaysia, Nepal, North Korea, Pakistan, Philippines, Sri Lanka, Taiwan Strait, Tajikistan, Thailand, Timor-Leste, Turkmenistan and Uzbekistan; in Europe, Armenia, Azerbaijan, Bosnia and Herzegovina, Cyprus, Georgia, Kosovo, Macedonia, North Caucasus, Serbia and Turkey; in the Middle East and North Africa, Algeria, Bahrain, Egypt, Iran, Iraq, Israel-Palestine, Jordan, Lebanon, Libya, Morocco, Syria, Tunisia, Western Sahara and Yemen; and in Latin America and the Caribbean, Colombia, Guatemala and Venezuela.

Crisis Group receives financial support from a wide range of governments, institutional foundations, and private sources. The following governmental departments and agencies have provided funding in recent years: Australian Agency for International Development, Austrian Development Agency, Belgian Ministry of Foreign Affairs, Canadian International Development Agency, Canadian International Development Research Centre, Royal Danish Ministry of Foreign Affairs, Dutch Ministry of Foreign Affairs, European Union Instrument for Stability, Finnish Ministry of Foreign Affairs, German Federal Foreign Office, Irish Aid, Principality of Liechtenstein, Luxembourg Ministry of Foreign Affairs, New Zealand Agency for International Development, Royal Norwegian Ministry of Foreign Affairs, Swedish International Development Cooperation Agency, Swedish Ministry of Foreign Affairs, Swiss Federal Department of Foreign Affairs, Turkish Ministry of Foreign Affairs, United Kingdom Department for International Development, U.S. Agency for International Development.

The following institutional and private foundations have provided funding in recent years: Adessium Foundation, Carnegie Corporation of New York, Elders Foundation, William and Flora Hewlett Foundation, Humanity United, Henry Luce Foundation, John D. and Catherine T. MacArthur Foundation, Oak Foundation, Open Society Foundations, Ploughshares Fund, Radcliffe Foundation, Rockefeller Brothers Fund, Stanley Foundation, The Charitable Foundation, Tinker Foundation Incorporated.

February 2013

Appendix D: Reports and Briefings on the Middle East and North Africa since 2010

Israel/Palestine

Tipping Point? Palestinians and the Search for a New Strategy, Middle East Report N°95, 26 April 2010 (also available in Arabic and Hebrew).

Drums of War: Israel and the "Axis of Resistance", Middle East Report N°97, 2 August 2010 (also available in Hebrew and Arabic).

Squaring the Circle: Palestinian Security Reform under Occupation, Middle East Report N°98, 7 September 2010 (also available in Arabic and Hebrew).

Gaza: The Next Israeli-Palestinian War?, Middle East Briefing N°30, 24 March 2011 (also available in Hebrew and Arabic).

Radical Islam in Gaza, Middle East/North Africa Briefing N°104, 29 March 2011 (also available in Arabic and Hebrew).

Palestinian Reconciliation: Plus Ça Change …, Middle East Report N°110, 20 July 2011 (also available in Arabic and Hebrew).

Curb Your Enthusiasm: Israel and Palestine after the UN, Middle East Report N°112, 12 September 2011 (also available in Arabic and Hebrew).

Back to Basics: Israel's Arab Minority and the Israeli-Palestinian Conflict, Middle East Report N°119, 14 March 2012 (also available in Arabic).

The Emperor Has No Clothes: Palestinians and the End of the Peace Process, Middle East Report N°122, 7 May 2012 (also available in Arabic).

Light at the End of their Tunnels? Hamas & the Arab Uprisings, Middle East Report N°129, 14 August 2012 (also available in Arabic).

Israel and Hamas: Fire and Ceasefire in a New Middle East, Middle East Report N°133, 22 November 2012 (also available in Arabic).

Extreme Makeover? (I): Israel's Politics of Land and Faith in East Jerusalem, Middle East Report N°134, 20 December 2012 (also available in Arabic).

Extreme Makeover? (II): The Withering of Arab Jerusalem, Middle East Report N°135, 20 December 2012 (also available in Arabic).

Egypt/Syria/Lebanon

Lebanon's Politics: The Sunni Community and Hariri's Future Current, Middle East Report N°96, 26 May 2010 (also available in Arabic).

New Crisis, Old Demons in Lebanon: The Forgotten Lessons of Bab-Tebbaneh/Jabal Mohsen, Middle East Briefing N°29, 14 October 2010 (only available in French and Arabic).

Trial by Fire: The Politics of the Special Tribunal for Lebanon, Middle East Report N°100, 2 December 2010.

Popular Protest in North Africa and the Middle East (I): Egypt Victorious?, Middle East/North Africa Report N°101, 24 February 2011 (also available in Arabic).

Uncharted Waters: Thinking Through Syria's Dynamics, Middle East Briefing N°31, 24 November 2011 (also available in Arabic).

Popular Protest in North Africa and the Middle East (VI): The Syrian People's Slow-motion Revolution, Middle East Report N°108, 6 July 2011 (also available in Arabic).

Popular Protest in North Africa and the Middle East (VII): The Syrian Regime's Slow-motion Suicide, Middle East Report N°109, 13 July 2011 (also available in Arabic).

Lebanon's Palestinian Dilemma: The Struggle Over Nahr al-Bared, Middle East Report N°117, 1 March 2012 (also available in Arabic).

Now or Never: A Negotiated Transition for Syria, Middle East Briefing N°32, 5 March 2012 (also available in Arabic and Russian).

Syria's Phase of Radicalisation, Middle East Briefing N°33, 10 April 2012 (also available in Arabic).

Lost in Transition: The World According to Egypt's SCAF, Middle East/North Africa Report N°121, 24 April 2012 (also available in Arabic).

Syria's Mutating Conflict, Middle East Report N°128, 1 August 2012 (also available in Arabic).

Tentative Jihad: Syria's Fundamentalist Opposition, Middle East Report N°131, 12 October 2012 (also available in Arabic).

A Precarious Balancing Act: Lebanon and the Syrian conflict, Middle East Report N°132, 22 November 2012 (also available in Arabic).

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