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The Iran-Libya Sanctions Act (ILSA)

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Summary

No firms have been sanctioned under the Iran-Libya Sanctions Act (ILSA), and it has terminated with respect to Libya. Renewed in August 2001 for another five years (P.L. 107-24), ILSA was scheduled to expire in August 2006. In the 109th Congress, H.R. 282 (passed by the House on April 26, 2006), S. 333, and H.R. 6198 would tighten some provisions. The latter, which extends ILSA until December 31, 2011, but allows substantial Administration flexibility, was passed and signed (P.L. 109-293). This report will be updated. See also CRS Report RL32048, *Iran: U.S. Concerns and Policy Responses*, by Kenneth Katzman.

Background and Original Passage of ILSA

ILSA was introduced in the context of a tightening of U.S. sanctions on Iran during the first term of the Clinton Administration. In response to Iran's stepped up nuclear program and its support to terrorist organizations (Hizbollah, Hamas, and Palestine Islamic Jihad), President Clinton issued Executive Order 12957 (March 15, 1995), which banned U.S. investment in Iran's energy sector, and Executive Order 12959 (May 6, 1995), which banned U.S. trade with and investment in that country. The Clinton Administration and many in Congress maintained that these sanctions would deprive Iran of the ability to acquire weapons of mass destruction (WMD) and to fund terrorist groups by hindering its ability to modernize its key petroleum sector. That sector generates about 20% of Iran's GDP. Iran's onshore oil fields, as well as its oil industry infrastructure, were aging and needed substantial investment, and its large natural gas resources (940 trillion cubic feet, exceeded only by those of Russia) were not developed at all at the time ILSA was first considered.

U.S. allies refused to sanction Iran in the mid-1990s, and the Clinton Administration and Congress believed that it might be necessary for the United States to try to deter foreign investment in Iran. The opportunity to do so came in November 1995, when Iran launched its first major effort to open its energy sector to foreign investment, which Iran had banned after the February 1979 Islamic revolution on the grounds that foreign firms would gain undue control over Iran's resources. To accommodate that philosophy while attracting needed foreign help, Iran developed a "buy-back" investment program under

which foreign firms recoup their investments from the proceeds of oil and gas discoveries but do not receive equity stakes.

As Iran was announcing its plans, some in Congress, with input from the Clinton Administration, developed legislation to sanction such investment. On September 8, 1995, Senator Alfonse D'Amato introduced the Iran Foreign Oil Sanctions Act of 1995 to sanction foreign firms' export to Iran of energy technology. The bill passed the Senate on December 18, 1995 (voice vote) but, in contrast to the introduced version, imposed sanctions on foreign *investment* in Iran's energy sector. The Clinton Administration was concerned that U.S. monitoring of foreign exports to Iran would be too difficult to implement. On December 20, 1995, the Senate passed still another version with an amendment, sponsored by Senator Edward Kennedy, that applied all provisions to Libya as well, which at the time was still refusing to yield for trial the two suspects in the December 21, 1988, bombing of Pan Am 103, both allegedly agents of Libyan intelligence. The House passed its version of the bill, H.R. 3107, on June 19, 1996 (415-0). The Senate passed a slightly different version on July 16, 1996 (unanimous consent); the House concurred, and the President signed it into law (P.L. 104-172, August 5, 1996).

ILSA was to sunset on August 5, 2001 (5 years after enactment), in the context of somewhat improved U.S. relations with both Iran and Libya. During 1999 and 2000, the Clinton Administration had eased the trade ban on Iran somewhat in response to the more moderate policies of Iran's President Mohammad Khatemi. In 1999, Libya yielded for trial of the Libyan suspects in Pan Am 103. However, proponents of ILSA renewal maintained that ILSA was slowing investment in both countries and that both would view ILSA's expiration as a concession, reducing their incentive for further moderation. Legislation to renew ILSA (H.R. 1954) was enacted in the 107th Congress (P.L. 107-24, August 3, 2001). The renewal law changed the definition of investment to treat any additions to pre-existing investment as a new investment, and required an Administration report on ILSA's effectiveness within 24 to 30 months of enactment; that report was submitted to Congress in January 2004 and did not recommend that ILSA be repealed.

Key Provisions

ILSA requires the President to impose at least two out of a menu of six sanctions on foreign companies (entities, persons) that make an "investment" of more than $20 million in one year in Iran's energy sector.[1] The six sanctions available (Section 6) are (1) denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports to the sanctioned entity; (2) denial of licenses for the U.S. export of military or militarily-useful technology to that entity; (3) denial of U.S. bank loans exceeding $10 million in one year to the entity; (4) if the entity is a financial institution, a prohibition on its service as a primary dealer in U.S. government bonds; and/or a prohibition on its service as a repository for U.S. government funds (each counts as one sanction); (5) prohibition on U.S. government procurement from the entity; and (6) a restriction on imports from the entity, in accordance with the International Emergency Economic Powers Act (IEEPA, 50 U.S.C. 1701 and following).

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[1] For Libya, the threshold was $40 million, and sanctionable activity included exportation to Libya of a broad range of technology of which the export to Libya was banned by Pan Am 103-related Security Council Resolutions 748 (Mar. 31, 1992) and 883 (Nov. 11, 1993).

Waiver/Expiration Provisions. The President may waive ILSA sanctions on Iran if the parent country of the violating firm agrees to impose economic sanctions on Iran (Section 4(c)) or if he certifies that doing so is important to the U.S. national interest (Section 9(c)). ILSA terminates for Iran if Iran ceases its efforts to acquire WMD and is removed from the U.S. list of state sponsors of terrorism. For Libya, ILSA terminates if the President determines that Libya has fulfilled the requirements of all U.N. resolutions relating to the downing of Pan Am 103. (President Bush made that certification on April 23, 2004, terminating ILSA for Libya.)

Implementation and Effectiveness

Traditionally skeptical of economic sanctions as a policy tool, the European Union states opposed ILSA as an extraterritorial application of U.S. law. The EU countries threatened formal counter-action in the World Trade Organization (WTO), and in April 1997, the United States and the EU formally agreed to try to avoid a trade confrontation over ILSA (and a separate "Helms-Burton" Cuba sanctions law, P.L. 104-114). The agreement contributed to a decision by the Clinton Administration to waive ILSA sanctions on the first project determined to be in violation: a $2 billion[2] contract, signed in September 1997, for Total SA of France and its minority partners, Gazprom of Russia and Petronas of Malaysia to develop phases 2 and 3 of the 25-phase South Pars gas field. The Administration announced the "national interest" waiver (Section 9(c) of ILSA) on May 18, 1998, after the EU pledged to increase cooperation with the United States on non-proliferation and counter-terrorism. The announcement indicated that EU firms would likely receive waivers for future projects that were similar.

As did its predecessor, the Bush Administration sought to work cooperatively with the EU to curb Iran's nuclear program and limit its support for terrorism rather than risk a rift by imposing sanctions on EU (or other) firms. Some believe ILSA did slow Iran's energy development initially, but, as shown by the projects agreed to below, its deterrent effect weakened as foreign companies began to perceive that ILSA sanctions would not likely be imposed. Since that sanctions waiver, about $11.5 billion in foreign investments in Iran's energy sector have been agreed to. The new investment has not boosted Iran's sustainable oil production significantly — it is still about 4 million barrels per day (mbd)[3] — but the foreign investment apparently has slowed any deterioration. In addition, Iran's gas sector, non-existent prior to the late 1990s, is becoming an increasingly important factor in Iran's energy future as a result of foreign investment.

Since the South Pars case, a number of investments in Iran have been formally placed under review for ILSA sanctions by the State Department (Bureau of Economic Affairs). State Department reports to Congress on ILSA, required every six months, state that U.S. diplomats raise U.S. policy concerns about Iran with both investing companies and their parent countries. However, no sanctions determinations have been announced since the South Pars case. **Table 1** shows reported post-1999 energy investments in Iran.

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[2] Dollar figures for energy investment contracts with Iran represent public estimates of the amounts investing firms are expected to spend during the life of the project, which might in some cases be several decades.

[3] Testimony of Deputy Assistant Secretary of State Anna Borg before the House International Relations Committee, Subcommittee on the Middle East and Central Asia. June 17, 2003.

Table 1. Post-1999 Foreign Investment in Iran Energy Sector

Date	Field	Company(ies)	Value	Output Goal
Feb. 1999	Doroud (oil)	Totalfina Elf/ENI	$1 billion	205,000 bpd
Apr. 1999	Balal (oil)	Totalfina Elf/ Bow Valley (Canada)/ENI	$300 million	40,000 bpd
Nov. 1999	Soroush and Nowruz (oil)	Royal Dutch Shell	$800 million	190,000 bpd
Apr. 2000	Anaran (oil)	Norsk Hydro (Norway)		
July 2000	Phase 4 and 5, South Pars (gas)	ENI	$1.9 billion	2 billion cu.ft./day
Mar. 2001	Caspian Sea oil exploration	GVA Consultants (Sweden)	$225 million	
June 2001	Darkhovin (oil)	ENI	$1 billion	160,000 bpd
May 2002	Masjid-e-Soleyman (oil)	Sheer Energy (Canada)	$80 million	25,000 bpd
Sep. 2002	Phase 9 and 10, South Pars (gas)	LG (South Korea)	$1.6 billion	
Oct. 2002	Phase 6, 7, 8, South Pars (gas)	Statoil (Norway)	$2.65 billion	3 billion cu.ft./day
Feb. 2004	Azadegan (oil) (Iran is threatening to cancel this deal as of October 2006 for Inpex's refusal to agree on final terms.)	Inpex (Japan)	$2 billion	300,000 bpd
Totals			**$11.5 billion**	**Oil: 920,000 bpd** **Gas: 5 billion cu.ft/day**

ILSA and Emerging Energy Relationships. ILSA's definition of "investment" does not specifically mention as violations of ILSA long-term oil or gas purchases from Iran, or the building of energy transit routes to or through Iran. However, the Clinton Administration position was that the construction of energy routes might violate ILSA, because these routes would "directly and significantly contribut[e] to the enhancement of Iran's ability to develop petroleum resources."[4] The Clinton Administration used that argument to deter energy routes involving Iran and thereby successfully promote an alternate Caspian energy route from Azerbaijan (Baku) to Turkey (Ceyhan). This route, which became operational in 2005, bypasses both Iran and Russia.

At the same time, the Clinton and Bush Administrations have adopted flexible interpretations of ILSA to accommodate the needs of key regional allies for energy supplies. A few weeks after ILSA was enacted, Turkey and Iran agreed to construct a natural gas pipeline from Iran to Turkey (each country constructing the pipeline on its side of their border). Turkey later announced that, at least initially, it would import gas only from Turkmenistan through this pipeline. In July 1997, the State Department said that the project did not violate ILSA because Turkey would be importing gas from Turkmenistan, not Iran, and the project would therefore not benefit Iran's energy sector directly. Direct Iranian gas exports to Turkey began in 2001, in apparent contravention of Turkey's pledges not to buy Iranian gas directly, but the Bush Administration has not imposed ILSA sanctions on the project.

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[4] This definition of sanctionable activity is contained in Section 5(a) of ILSA.

Further tests of ILSA are looming as Pakistan, India and China build energy ties to Iran; some deals might include pipeline projects to Iran. In October 2004, Iran negotiated a long-term agreement to allow China (Sinopec) and India (Oil and Natural Gas Corp., ONGC) to develop Iran's Yadavaran oil field, which might be able to produce 300,000 barrels per day, in exchange for agreeing to purchase 10 million tons of Iranian LNG annually for 25 years. Under the preliminary agreement, Sinopec would obtain a 51% stake in Yadavaran and ONGC would get a 20% stake. Iran's National Iranian Oil Company would obtain the remaining stake. In February 2006, China and Iran tried to finalize the deal in advance of any potential United Nations sanctions that might be imposed on Iran for its nuclear program. A related deal would allow the state-owned Indian Oil Company to develop part of South Pars and build an LNG plant in Iran. If implemented for the full duration of the agreements, these deals could total over $100 billion, although some question whether such deals would go to their full term.

The agreements to import Iranian LNG would not appear to constitute an "investment" in Iran's energy sector, as defined by ILSA. However, a related aspect of these deals, particularly those involving Indian firms,[5] is the construction of a gas pipeline from Iran to India, through Pakistan, with a possible extension to China. All three governments have repeatedly reiterated their commitment to the $4 billion to $7 billion project, which is planned to begin construction in 2007 and to be completed by 2010. Pakistan's President Musharraf said in January 2006 that there is enough demand in Pakistan for Iranian gas to make the project feasible, even if India declines to join it. During her visit to Asia in March 2005, Secretary of State Rice "expressed U.S. concern" about the pipeline deal; other U.S. officials have called the project "unacceptable." No U.S. official has directly stated that it would be considered a violation of ILSA. During his trip to India and Pakistan in March 2006, President Bush said the United States "understand[s]" Pakistan's need for gas, appearing to suggest he would not oppose the pipeline, but Administration officials later said that there was no change in Administration opposition to it. Aside from commercial considerations, the volatility of relations between India and Pakistan, particularly the status of Jammu and Kashmir, could derail the project at any time. A House resolution (H.Res. 353), introduced July 11, 2005, expresses support for the gas pipeline project as a facilitator of India-Pakistan peace.

Proposed ILSA Modifications and Extensions

ILSA was to terminate on August 5, 2006, unless renewed by Congress. ILSA-related legislation in the 109th Congress includes the Iran Freedom and Support Act of 2005, H.R. 282 (Ros-Lehtinen) and a companion, S. 333 (Santorum). These bills would not only extend ILSA (indefinitely) but would also close some perceived ILSA loopholes and authorize funding for pro-democracy activities in Iran. A House bill, H.R. 6198, similar to H.R. 282 but, as discussed below, allowing more Administration flexibility, was introduced on September 27, 2006. H.R. 282 was reported out by the House International Committee on March 15, 2006, by a vote of 37-3, with slight amendment.

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[5] Some of the Indian companies that reportedly might take part in the pipeline project are ONGC Corp.; GAIL Ltd.; Indian Oil Corp.; and Bharat Petroleum Corp. Some large European companies have also expressed interest. See Solomon, Jay and Neil King. "U.S. Tries to Balance Encouraging India-Pakistan Rapprochement With Isolating Tehran." *Wall Street Journal*, June 24, 2005, p. A4.

The House passed it on April 26, 397-21. S. 333 had 61 co-sponsors as of June 21, but a version of the bill, submitted as an amendment to the FY2007 defense authorization bill (S. 2766), was not adopted (June 14). To prevent ILSA expiration while these bills were being further considered, H.R. 5877, extending ILSA until September 29, 2006, was passed by both chambers and signed on August 4, 2006 (P.L. 109-267). A Senate bill, S. 2657, would extend ILSA until August 5, 2011. The most significant ILSA-related provisions of the bills are as follows:

- increasing the requirements on the Administration to justify waiving sanctions on companies determined to have violated ILSA provisions (under Section 4(c) of ILSA, referring to parent countries' cooperation with U.S. sanctions on Iran);
- making exports to Iran of WMD-useful technology or "destabilizing numbers and types of" advanced conventional weaponry sanctionable;
- setting a 90-day time limit (urging a 180-day limit in H.R. 6198) for the Administration to determine whether an investment constitutes a violation of ILSA. (There was no time limit previously); and
- increasing the threshold for terminating ILSA by requiring the Administration to certify, in addition to existing termination requirements, that Iran "poses no threat" to the United States, its interests, and its allies.

H.R. 282 and H.R. 6198 also

- cut U.S. foreign assistance to countries whose companies have violated ILSA's provisions (H.R. 282) or recommend against U.S. nuclear agreements with countries that have supplied nuclear technology to Iran (H.R. 6198);
- apply ILSA's provisions to foreign subsidiaries of U.S. companies (H.R. 282 only); and
- require public disclosure of investment funds that have investments in companies that have invested in Iran's energy sector (H.R. 282 only);

In addition, H.R. 6198 would extend ILSA until December 31, 2011, and contains a provision to try to prevent money-laundering by criminal groups, terrorists, or entities involved in proliferating WMD. It also drops Libya from ILSA, as requested by the Administration. H.R. 6198 was passed by voice vote and unanimous consent in the House (September 28) and Senate (September 30). The Administration had opposed H.R. 282 and S. 333 on the grounds that Administration flexibility would be limited and the bills would hurt the U.S. effort to work with its allies to curb Iran's nuclear program. Supporters of these bills believe that continued investment in Iran's energy sector undermines containment of Iran's nuclear program. In part because H.R. 6198 gives the Administration more flexibility than did the other bills, President Bush signed it into law on September 30, 2006 (P.L. 109-293).