Order Code RS20871
Updated July 9, 2007

CRS Report for Congress

The Iran Sanctions Act (ISA)

Kenneth Katzman
Specialist in Middle Eastern Affairs
Foreign Affairs, Defense, and Trade Division

Summary

No firms have been sanctioned under the Iran Sanctions Act (ISA). Set to expire in August 2006, legislation in the 109th Congress (the "Iran Freedom Support Act, P.L. 109-293) extended it until December 31, 2011, terminated application to Libya, and added provisions, although with substantial Administration flexibility in implementation. Proposed ISA-related legislation in the 110th Congress, such as H.R. 1400, would remove some of that flexibility. See also CRS Report RL32048, *Iran: U.S. Concerns and Policy Responses*, by Kenneth Katzman.

Background and Original Passage of ISA

The Iran Sanctions Act, originally called the Iran-Libya Sanctions Act (ILSA), was introduced during a tightening of U.S. sanctions on Iran during 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), banning U.S. investment in Iran's energy sector, and Executive Order 12959 (May 6, 1995), banning U.S. trade with and investment in Iran. The Clinton Administration and Congress maintained that these sanctions would curb the strategic threat from Iran by hindering its ability to modernize its key petroleum sector, which generates about 20% of Iran's GDP. Iran's onshore oil fields, as well as its oil industry infrastructure, are aging and need 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 ISA 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 their 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. To accommodate Iran's philosophy to retain control of its national resources, Iran developed a "buy-back" investment program in which foreign firms recoup their investments from the proceeds of oil and gas discoveries but do not receive equity stakes.

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' exports to Iran of energy technology. The bill passed the Senate on December 18, 1995 (voice vote) but, in consideration of the difficulty of monitoring foreign exports to Iran, sanctioned foreign *investment* in Iran's energy sector. On December 20, 1995, the Senate passed another version applying all provisions to Libya as well, which was refusing to yield for trial the two Libyan intelligence agents suspected in the December 21, 1988, bombing of Pan Am 103. The House passed its version of the bill, H.R. 3107, on June 19, 1996 (415-0), and then concurred on a slightly different Senate version adopted on July 16, 1996 (unanimous consent). It was signed on August 5, 1996 (P.L. 104-172).

Key Provisions. ISA requires the President to impose at least two out of a menu of seven 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 sanctions (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 the 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 serving 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) restriction on imports from the entity, in accordance with the International Emergency Economic Powers Act (IEEPA, 50 U.S.C. 1701 and following). In the original law, the President may waive the 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)). It terminated application to Iran if Iran ceases its efforts to acquire WMD and is removed from the U.S. list of state sponsors of terrorism. Its application to Libya terminated when the President determined on April 23, 2004, that Libya had fulfilled the requirements of all U.N. resolutions on Pan Am 103.

Traditionally skeptical of economic sanctions as a policy tool, European Union states opposed ISA as an extraterritorial application of U.S. law and threatened counter-action in the World Trade Organization (WTO). In April 1997, the United States and the EU formally agreed to try to avoid a trade confrontation over it (and a separate "Helms-Burton" Cuba sanctions law, P.L. 104-114). The agreement contributed to a May 18, 1998, decision by the Clinton Administration to waive ILSA sanctions ("national interest" grounds — Section 9(c)) 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. For its part, the EU pledged to increase cooperation with the United

---

[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 (March 31, 1992) and 883 (November 11, 1993).

[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.

States on non-proliferation and counter-terrorism. The Administration indicated that EU firms would likely receive waivers for future similar projects.

ISA 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 renewal maintained that both countries would view its expiration as a concession. Renewal legislation was enacted in the 107th Congress (P.L. 107-24, August 3, 2001); it changed the definition of investment to treat any additions to pre-existing investment as new investment, and required an Administration report on ISA's effectiveness within 24 to 30 months of enactment. That report was submitted to Congress in January 2004 and did not recommend that ISA be repealed.

Modifications in the 109th Congress

During the 109th Congress, with U.S. concern about Iran's nuclear program increasing, ISA was to terminate on August 5, 2006. Some Members, concerned that its provisions were not being applied to purported violators because of Administration diplomatic considerations, introduced the "Iran Freedom and Support Act" (H.R. 282, S. 333) to extend ISA indefinitely, to close some perceived loopholes, and to authorize funding for pro-democracy activities in Iran. These bills increased the requirements on the Administration to justify waiving sanctions on companies determined to have violated ISA, made exports to Iran of WMD-useful technology or "destabilizing numbers and types of" advanced conventional weaponry sanctionable, set a 90-day time limit for the Administration to determine whether an investment constitutes a violation of ISA (there is no time limit in the original law), and increased the threshold for terminating ISA. H.R. 282 also cut U.S. foreign assistance to countries whose companies have violated ISA and applied the U.S. trade ban on Iran to foreign subsidiaries of U.S. companies. H.R. 282 was reported out by the House International Committee on March 15, 2006, by a vote of 37-3, with slight amendment. The House passed it on April 26, 397-21. S. 333 had 61 co-sponsors as of June 21, 2006. To prevent ISA expiration while these bills were being considered, H.R. 5877, extending it until September 29, 2006, was passed and signed on August 4, 2006 (P.L. 109-267).

Toward the end of the 109th Congress, H.R. 6198, a modified version of H.R. 282, was introduced to address Administration concerns that H.R. 282 and S. 333 did not allow sufficient Administration flexibility. It made sanctionable sales of WMD-useful technology or "destabilizing numbers and types of" advanced conventional weapons and adds a required determination that Iran "poses no significant threat" in order to terminate application to Iran, a provision close to that contained in H.R. 282. It recommended, but did not require, a 180-day time limit for a determination of violation and changed the multi-lateral sanctions waiver provision ("4(c) waiver," see above) to a national security interest waiver. The law also recommended against U.S. nuclear agreements with countries that have supplied nuclear technology to Iran, extended ISA until December 31, 2011, dropped Libya from ISA, and contained a provision to try to prevent money-laundering by criminal groups, terrorists, or proliferators. It was passed by the House and Senate by voice vote and unanimous consent, respectively, and was signed on September 30, 2006 (P.L. 109-293). It changed the name of ILSA to the Iran Sanctions Act (ISA).

Effectiveness and Ongoing Challenges

Some believe ILSA slowed Iran's energy development initially, but, as shown by the projects agreed to below, its deterrent effect appeared to weaken as foreign companies began to perceive that sanctions could be avoided. The projects listed are said to be under review for ISA sanctions by the State Department (Bureau of Economic Affairs), but no determinations have been announced. State Department reports to Congress on ISA, required every six months, state that U.S. diplomats raise U.S. policy concerns about Iran with both investing companies and their parent countries. Most of the projects agreed before 2004 are underway and, in many cases, now producing gas or oil. Still, some energy experts believe that investment would have been much more extensive if not for both ISA as well as Iran's purported aggressive negotiating style. The new investment has not boosted Iran's sustainable oil production significantly — it is still about 4 million barrels per day (mbd)[3] — and an analysis published by the National Academy of Sciences says that Iranian oil exports are declining to the point where Iran might have negligible exports of oil by 2015.[4] Some questioned the study's conclusions, and others maintain that Iran's gas sector, virtually non-existent in 1998, is becoming an increasingly important factor in Iran's energy future as a result of foreign investment.

ISA's definition of "investment" does not specifically mention oil or gas purchases from Iran, or the building of energy transit routes to or through Iran. However, the Clinton and Bush Administration position has been that the construction of energy routes would violate the law, because these routes would "directly and significantly contribut[e] to the enhancement of Iran's ability to develop petroleum resources."[5] The Clinton Administration used that argument to deter energy routes involving Iran and thereby successfully promote an alternate route from Azerbaijan (Baku) to Turkey (Ceyhan). This route became operational in 2005. However, neither Administration imposed sanctions on another project viewed as beneficial to U.S. ally Turkey: a natural gas pipeline from Iran to Turkey (each country constructing the pipeline on its side of their border). In July 1997, the State Department said that the project did not violate ISA because Turkey would be importing gas from Turkmenistan, not Iran, and would therefore not benefit Iran's energy sector directly. However, direct Iranian gas exports to Turkey began in 2001, in apparent contravention of Turkey's pledges. It is not clear whether or not Iranian investments in energy projects in other countries, such as reputed Iranian investment to help build five oil refineries in Asia (China, Indonesia, Malaysia, and Singapore) and in Syria, would constitute sanctionable investment under ISA.

Further tests of ISA are looming, and some of the large, long-term deals between Iran and Indian, Chinese, and Malaysian firms, listed below, have the potential to significantly enhance Iran's energy export prospects. On the other hand, some of these deals are believed to be preliminary agreements that might not necessarily be implemented. Most of the value of these agreements includes long-term contracts to purchase Iranian oil and

---

[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.

[4] Stern, Roger. "The Iranian Petroleum Crisis and United States National Security," *Proceedings of the National Academy of Sciences of the United States of America*. December 26, 2006.

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

gas, and the exact investment amounts for the exploration and production phases of these projects are not known. A related deal, particularly those involving Indian firms,[6] 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. Since January 2007, the three countries have agreed on various outstanding issues, including a pricing formula and the Indian and Pakistani split of the gas supplies, but talks continue on several unresolved issues, including the pipeline route, security, transportation tariffs, and related issues. U.S. officials, including Secretary of State Rice, have "expressed U.S. concern" about the pipeline deal or have called it "unacceptable," but no U.S. official has stated outright that it would be sanctioned.

ISA is not the only mechanism available to the United States to try to limit investment in Iran. Undersecretary of State Burns told Congress on March 29, 2007, that U.S. officials are having some success persuading European governments to limit new export credits guarantees to Iran. This result is due not only to U.S. diplomacy but also to U.S. presentations of the financial risk posed by providing credit to Iran. The Organization for Economic Cooperation and Development (OECD) in 2006 raised the financial risk rating for Iran. The U.S. Treasury and State Departments have begun using U.S. financial regulations in an apparently successful effort to pressure European banks not to provide letters of credit for exports to Iran or to process dollar transactions for Iranian banks. Undersecretary of State Burns and Undersecretary of the Treasury Stuart Levey testified on March 21, 2007, that "... many leading foreign banks have either scaled back dramatically or terminated entirely their Iran-related business ... concluding that they simply did not wish to be a banker for a regime that deliberately conceals the nature of its illicit business." The restrictions on financing are, according to Iranian and outside observers, making it more difficult to fund energy industry and other projects in Iran.

Proposed Further Amendments

In the 110th Congress, H.R. 1400 contains numerous provisions, some of which pertain to ISA, others of which do not. For all its major provisions, see CRS Report RL32048, *Iran: U.S.Concerns and Policy Responses*. Among ISA-related provisions, H.R. 1400 would remove the Administration's ability to waive application of sanctions under ISA under Section 9(c), national interest grounds. However, the bill would not impose on the Administration a time limit to determine whether a project is sanctionable. Both it and other bills, its Senate counterpart S. 970, and another House bill, H.R. 957, would expand the definitions of sanctionable entities to official credit guarantee agencies, such as France's COFACE and Germany's Hermes, and apply ISA sanctions to investment in Iran's efforts to develop a liquified natural gas (LNG) sector; Iran currently has no LNG export terminals. H.R. 1400 also would require the President to impose the ban on U.S. procurement from any entity sanctioned under ISA, and impose one other of the menu of sanctions. Another bill, H.R. 1357, would require government pension funds

---

[6] 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.

to divest of shares in firms that have made ISA-sanctionable investments in Iran's energy sector, and call on private pension funds to divest as well. H.R. 2880 would make sanctionable any sales to Iran of refined petroleum resources after December 31, 2007. This latter bill apparently seeks to express support for possible U.N. Security Council sanctions, said to be under consideration, to ban gasoline sales to Iran.

Post-1999 Foreign Investment in Iran's Energy Sector

Date	Field	Company(ies)	Value	Output Goal
Feb. 1999	Doroud (oil)	Totalfina Elf (France)/ENI (Italy)	$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)	Inpex (Japan) 10% stake	$200 million Japan stake	260,000 bpd
Oct. 2004	Yadavaran (oil); deal includes gas purchases for 30 years	Sinopec (China) and ONGC (India)	$70 billion (value of exploration not known)	300,000 bpd
June 2006	Gamsar block (oil)	Sinopec (China)	$50 million	?
Totals			**$80 billion+**	**Oil: 1.2 million bpd Gas: 5 billion cu.ft/day+**
Pending Deals/Preliminary Agreements				
Golshan and Ferdows (offshore gas, includes downstream development and transportation)		SKS Ventures (Malaysia)	$20 billion	100 million cu.ft/day
North Pars Gas Field (offshore gas)		China National Offshore Oil Co.	$16 billion (includes purchases of the gas	3.6 billion cu.ft/day
Phase 13 and 14 - South Pars (gas); includes building a liquified natural gas (LNG) terminal		Royal Dutch Shell and Repsol (Spain)	$10 billion	?