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Policy Alert

The IRGC May Try to Divert Iraq's Electricity Payments

by Michael Knights (/experts/michael-knights)

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Brief Analysis

As Baghdad prepares to send large back payments to Tehran, any misappropriation could threaten the flow of electricity to Iraq and bolster sanctioned entities in Iran.

Iraq and Iran's close trading ties are heavily unbalanced in Tehran's favor—$6.5 billion of Iranian exports to Iraq versus $60 million in the other direction. This disparity extends to electricity, where Iran currently provides 5.9 percent of its neighbor's power supplies, according to Iraq's Ministry of Electricity. Although more expensive than domestically produced electricity, the Iranian supply has helped prop up Iraq's slowly recovering power sector since 2003.

Under normal circumstances, such trade would not merit outside scrutiny so long as Iraq avoids dealing with sanctioned Iranian actors. But with **Iran's currency depreciating (http://www.washingtoninstitute.org/policy-analysis/view/mismanagement-leaves-irans-economy-vulnerable)** , and with the Islamic Revolutionary Guard Corps (IRGC) spending more than $6 billion per year (according to a UN estimate) to prop up the Syrian regime, there is a growing risk that sanctioned entities will seek to siphon off large injections of foreign currency. Iraq's forthcoming electricity payments may therefore be a key test of Tehran's ability to direct foreign payments where they are supposed to go, and of the international community's ability to monitor such transfers.

Tavanir, a specialized holding company owned almost entirely by Iran's Ministry of Energy, has negotiated annual electricity export deals with Iraq since 2013. The firm negotiates tariffs on behalf of the regional electricity generation companies that provide power to Iraq; it also transfers payments to them.

Facing the twin blow of war against the Islamic State and an oil price crash, Iraq has struggled to pay its monthly $100 million electricity bill to Tehran. In April 2015, as Iraqi forces pushed the terrorist group back from the outskirts of Baghdad, Iran cut off power exports for seven months. The flow was restored at the beginning of 2016, but Iraq made only three payments that year. The arrears eventually piled up to $1.3 billion, and Iran cut off electricity supplies again when the contract lapsed that December. Between April and July 2017, however, Baghdad made payments of $500 million. And on March 8, 2018, Iran agreed to supply 1,000 megawatts for another year. Iraq sent a $100 million payment to Tavanir this week, and new payments of $200-300 million are expected in the coming weeks.

The timing is critical for Tavanir, which has accrued debts of around $5 billion to regional electricity companies and desperately needs to be paid. Three of these companies provide electricity to Iraq—Behbahan, Manshahr, and Dalahu—but they have had difficulty paying worker salaries and keeping up with maintenance due to Tavanir's underpayments.

For the sake of Baghdad and other U.S. allies, it is important that Tavanir transfer incoming Iraqi money to these regional companies promptly and directly. Tavanir has numerous international partners—including its $10 billion strategic lender, South Korea's KEPCO—that have a lot to lose if the company interacts with sanctioned entities. The stakes for Iraq are even higher. The country needs dependable power supplies to continue its recovery from years of war and foster social stability, especially ahead of next month's parliamentary elections. The IRGC no doubt hopes to influence those elections via its powerful political and militia proxies in Iraq. At a time when the financial cost of the Syria war is bleeding the organization white, IRGC officials may see Baghdad's electricity payments as a potential source of additional money for supporting Iraqi proxies before and after the vote.

Given President Trump's recent political appointments and other developments, **Washington seems poised (http://www.washingtoninstitute.org/policy-analysis/view/how-will-iran-prepare-for-potential-u.s.-withdrawal-from-the-jcpoa)** to launch a more active strategy for countering and pressuring Iran, which may mean enhanced scrutiny of financial transfers to regime institutions and their associated companies. All eyes should therefore be focused on Iraq's electricity payments in the coming months, monitoring them for potential diversion. If Baghdad clears its debt to Iran's regional electricity companies, one might expect to see each firm improve its salary payments and maintenance operations. If not, then these indicators and other intelligence may point to payments being diverted to the IRGC. The U.S. Treasury and State Departments should work with Tavanir's foreign partners, such as the South Korean government and banks, to ensure that sanctioned entities are not interposing themselves into energy transactions.

In the longer term, Washington should help Iraq redress its alarming imbalance of trade with Iran. Iraqi farmers have been undermined for a decade-and-a-half by open borders and the food-dumping practices of Iranian traders; the country's manufacturing has likewise suffered. In the near term, though, the U.S.-Iraq Strategic Framework Agreement should prioritize support on electricity issues, so that Baghdad can phase out imported Iranian supplies by ramping up its own efforts to generate, transmit, and distribute power while implementing subsidy reform programs. Bilateral collaboration under the framework should also help Iraq accelerate its plan to end expensive purchases of Iranian natural gas, which costs the country $11.23 per thousand cubic feet (compared to the $6.50 that Europe pays for more-distant gas imports from Russia). This means helping Baghdad make better use of the estimated 565 million cubic feet of domestic gas **it currently wastes each year (http://www.washingtoninstitute.org/policy-analysis/view/iraqs-energy-future-lies-to-the-north)** through flaring.

Michael Knights is a Lafer Fellow with The Washington Institute. ❖

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