

Make Iran Feel the Pain

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Articles & Testimony

The international community, led by the U.S. and the U.K., is now developing and debating new economic sanctions against Iran. This third round will be pivotal -- either by significantly increasing the cost to Iran of continuing to engage in illicit and dangerous activities, or by showing the regime that it can outlast whatever symbolic measures are levied against it without fear of being bled financially.

The first two rounds of targeted and graduated sanctions have failed to change Iran's nuclear calculus. Iran's chief nuclear negotiator continues to meet with senior EU officials, most likely to buy time, while Tehran refuses to accede to demands that it freeze its uranium enrichment program.

U.N. Security Council Resolutions 1737 and 1747, passed last December and March respectively, signaled seriousness about using financial measures against Iran. The first declared an international consensus to sanction Iran, and the second to target banks. In particular, Russian and Chinese support for these resolutions shocked Iran's President Mahmoud Ahmadinejad. Iran saw first-hand the weak U.N. pressure on Saddam Hussein and expected no worse treatment. Mr. Ahmadinejad reportedly predicted that neither Moscow nor Beijing would sign off on these resolutions. Their passage made the country's professional classes, which are proud of Iran's integration in the international system, feel the sting of diplomatic and economic isolation.

The most effective U.N. sanction was against Bank Sepah. Iran's fourth-largest and one of the most important financial institutions was shut out of the international financial system. But the package of measures was noteworthy less for the list of specific individuals and entities sanctioned than for starting a graduated process intended to force the regime to stop its illicit conduct.

For graduated sanctions to be effective, however, each deadline that passes without a change in Iran's behavior must be followed by another, more severe round of sanctions. To date, sanctions have had a primarily psychological impact, producing discontent within the powerful merchant (bazaari) classes and civil servants. Now the teeth must come out. Failure to follow up with tougher sanctions would undermine whatever progress sanctions have had to date.

So this third round is the moment of truth. The danger is that today's diplomacy produces only more symbolic measures, watered down by multilateral negotiations whose goal is international consensus.

To avoid such failure, this round should fill the gaps left open by the first two U.N. resolutions. Specifically, it can target additional Iranian banks, and focus on companies controlled by the Iranian Revolutionary Guard Corps, especially those involved in the oil and gas sectors.

The next resolution must also close loopholes like the lack of a mandatory travel ban on designated Iranian officials. It should include a two-way arms embargo banning not only the export of arms from Iran but also the importation of arms to Iran. And it should create a U.N. monitoring team, preferably based in Dubai, to ensure member states comply with the U.N. sanctions regime. It should also add to the U.N. list the 23 Iranian persons and entities subjected to asset forfeiture abroad by the EU but not the U.N. Another useful tool would be to require strict

inspections of all Iranian ships and aircraft to prevent violations of the arms ban or the import of banned or dual-use goods intended for Iran's nuclear program.

U.N. sanctions freezing the overseas assets of Bank Sepah were the first significant step toward isolating Iran from the international financial system. Sepah had facilitated the Iranian-North Korean missile procurement business and tried to conceal its role in these transactions.

Several additional Iranian banks are likely candidates to have their funds frozen overseas and slapped with a ban on doing business with them:

- Bank Melli was implicated in the December 2005 U.S. government fine of Dutch bank ABN Amro for violating the Iran/Libya Sanctions Act. Investigators found that Bank Melli used ABN Amro's Dubai office to conceal its role in illegal (under U.S. law) bank transfers to Iran.
- Bank Saderat was shut out of the U.S. financial system last September for its role in financing terrorism, including the transfer of tens of millions of dollars through branches in Europe to Lebanon's Hezbollah and EU-designated Palestinian terrorist groups like Hamas.
- U.S. Treasury officials have also cited the Central Bank of Iran as one of the state-owned banks that ask financial institutions to conceal their involvement in facilitating missile procurement, nuclear programs and terror financing.

Beyond banks, the next sanctions resolution must target the massive military-industrial complex controlled by the Iranian Revolutionary Guards, an elite paramilitary force. Considered the foundation of President Ahmadinejad's political powerbase, the Guards are also deeply involved in the country's proliferation activities. It also maintains a special branch -- the Qods Force -- responsible for arming, training and supporting terrorist groups like Hezbollah and Hamas and insurgents attacking Coalition and Iraqi forces in Iraq.

The Revolutionary Guards are primarily self-funded, with annual revenues from its businesses empire estimated at \$1 billion and expected to rise to \$1.5-\$2 billion with new projects awarded since Mr. Ahmadinejad came to power. According to the U.S. State Department, the Guards are "taking on an increasingly influential role in Iran's economy, with IRGC-affiliated companies winning important government contracts." Freezing the assets of industries controlled by them, like the behemoth engineering firm Khatam ol-Anbia, would resonate with the merchant class that is already critical of the Guards' exclusive access to no-bid contracts.

Moreover, while the prospect of directly sanctioning Iran's oil industry makes the crude markets jittery, the reality is that international economic sanctions will ultimately only be successful if they impact Iran's lucrative oil and gas industries. Going after Khatam ol-Anbia, which was recently awarded a \$2.09 billion contract by the Iranian government to develop parts of the South Pars natural gas field and a \$1.3 billion contract to build parts of a pipeline, would be a strong shot across the bow of the Iranian oil industry. Such contracts would be put in jeopardy by U.N. sanctions, since no international company could legally do business with a company like Khatam ol-Anbia.

Referring to the unanimously passed sanctions resolutions, President Ahmadinejad recently warned the international community "not to play with the lion's tail." But Iran, unlike North Korea, is well integrated into the world economy and vulnerable to economic sanctions that shut the regime out of the international financial system. Iran can survive a pesky, symbolic sanctions regime like a lion swatting flies with its tail. The regime couldn't easily ignore sanctions with real teeth.

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(<http://www.washingtoninstitute.org/templateC04.php?CID=265>) (Yale University Press, 2006). ❖

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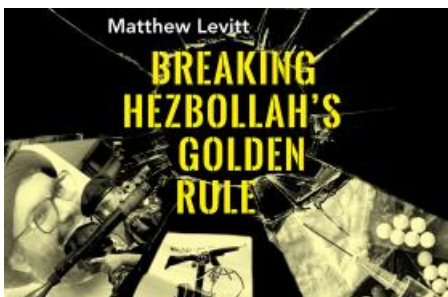
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