

The Implications of U.S. Aircraft Sales to Iran

Testimony before the Financial Services Committee,
Subcommittee on Monetary Policy and Trade

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I. Introduction

Chairman Huizenga, Vice Chairman Mulvaney, Ranking Member Moore, and distinguished members of the Financial Services Committee, Subcommittee on Monetary Policy and Trade, thank you for the opportunity to appear before you today to discuss the implications of U.S. aircraft sales to Iran.

Last year, the United States and its partners in the P5+1 realized a significant diplomatic accomplishment when they agreed to the Joint Comprehensive Plan of Action (JCPOA) with Iran.¹ In the JCPOA, Iran committed that it would never seek, develop, or acquire nuclear weapons. This agreement marks the first time in a decade that Iran accepted constraints on its nuclear program.

The agreement does not resolve all of the United States' or the international community's concerns about Iran's behavior. Indeed, Iran remains one of the principal strategic adversaries of the United States in the Middle East. Since 1984, Iran has been and remains designated as a state sponsor of terrorism; it provides substantial support to the regime of Bashar al-Assad in Syria's brutal civil war; it routinely engages in human rights abuses; and it continues its support for terrorist groups and non-state actors like Hezbollah and the Houthi rebels in Yemen that undermine the stability of governments throughout the Middle East. Until the adoption of the JCPOA last year, Iran's pursuit of an advanced nuclear program compounded the threat Iran posed to its regional neighbors and American interests in the stability of the Middle East.

Seen in this context, the JCPOA ameliorates one of the most important components of the threat from Iran—namely the menace posed by Iran's nuclear program and the possibility that its nuclear program could have been used to intensify the other ways in which Iran threatens the U.S., its allies, and its interests. Under the JCPOA, Iran agreed to relinquish a credible nuclear weapons option for at least the next decade and perhaps beyond in exchange for relief from most international and some U.S. sanctions.

While Iran retains the ability to enrich uranium subject to international supervision, the JCPOA imposed limitations on the number of centrifuges that Iran may operate; imposed limitations on the amount of enriched uranium Iran can keep in the country at any given time; and imposed limitations on permissible research and development into future nuclear capabilities. Iran also agreed to significant modifications to existing nuclear facilities, and to stringent monitoring and verification procedures, supervised by the International Atomic Energy Agency (IAEA). Left to develop its nuclear program free of international constraints, the threats posed by Iran's nuclear program and its other destabilizing activities would have been magnified. And there was a significant chance that Iran's further development of its nuclear program could have sparked a nuclear arms race throughout the Middle East.

¹ The P5+1 is the Permanent Five Members of the Security Council (China, France, the United States, United Kingdom, and Russia) plus Germany.

With the JCPOA, the threat posed by Iran’s nuclear program has been dramatically reduced, while the United States and its allies retain the ability to challenge Iran’s other destabilizing activities with all of the national security tools available, including sanctions. Indeed, the day after the JCPOA’s Implementation Day, the U.S. imposed sanctions on 11 individuals and entities responsible for supporting Iran’s ballistic missile program.² In March, individuals were designated for providing support to Iran’s ballistic missile program and to Iran’s Mahan Air, which itself was designated for providing support to the Islamic Revolutionary Guard Corps—Qods Force (IRGC—QF).³ And the Treasury Department has taken several actions to target the financial support networks of Hezbollah, including through the publication of regulations to implement the Hezbollah International Financing Prevention Act of 2015.⁴

The JCPOA imposes meaningful limitations on Iran’s nuclear program, lengthening the time needed for Iran to “break out” to a nuclear weapon from an estimated two to three months at the time the JCPOA was signed, to one year under the terms of the agreement.⁵ The JCPOA also engages a wide range of countries—including Russia and China—in the vision of a world in which Iran’s nuclear program is limited by agreement among the international community. As long as Iran adheres to the terms of the agreement, the JCPOA has significant value in the U.S.’s overall national security strategy, even while the U.S. acts to limit Iran’s malign influence through other means. And for the credibility of American commitments in a range of contexts the United States must adhere to the agreements it strikes with adversaries and allies alike as long as its counterparts do so as well. We must, therefore, work to maintain the integrity and viability of the JCPOA and resist efforts to undermine it so long as Iran fulfills its end of the bargain.

II. The Road to the JCPOA

Agreement by the P5+1 and Iran to the JCPOA was the culmination of a broad multi-year campaign that used sanctions and other forms of coercive diplomacy to incentivize Iran to engage in negotiations over its nuclear program. While the United States led this effort, it worked closely with allies and partners around the world. And Congress and the Executive Branch—across both the Bush and Obama administrations—played complementary roles in generating the leverage necessary to reach an agreement. Iran’s own economic challenges, stemming from a range of sources, also increased its incentives to agree to limits on its nuclear program in exchange for sanctions relief.

² “Treasury Sanctions Those Involved in Ballistic Missile Procurement for Iran,” U.S. Department of the Treasury, press release, January 17, 2016, <https://www.treasury.gov/press-center/press-releases/Pages/jl0322.aspx>.

³ “Treasury Sanctions Supporters of Iran’s Ballistic Missile Program and Terrorism-Designated Mahan Air,” U.S. Department of the Treasury, press release, March 24, 2016, <https://www.treasury.gov/press-center/press-releases/Pages/jl0395.aspx>.

⁴ Publication of the Hizballah International Financing Prevention Act of 2015 Related Sanctions Regulations; Counter Terrorism Designations Updates; Syria Designations Updates,” U.S. Department of the Treasury, April 15, 2016, <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20160415.aspx>.

⁵ “The Historic Deal that Will Prevent Iran from Acquiring a Nuclear Weapon,” The White House, Jan. 16, 2016, <https://www.whitehouse.gov/issues/foreign-policy/iran-deal>.

The pressure campaign on Iran to change its calculations about its nuclear program had three main components—U.S. sanctions that set the standard both for generating leverage against Iran and for revealing Iran’s deceptive conduct; complementary actions taken by our allies and partners, particularly the EU; and restrictions embodied in U.N. Security Council Resolutions. By the end of 2013 the combined efforts of these parties culminated in an interim agreement between Iran and the P5+1, the Joint Plan of Action (JPOA). The JPOA provided Iran limited sanctions relief in exchange for freezing its nuclear program while a permanent agreement was negotiated. The JPOA was renewed several times until July 2015 when the JCPOA was finally agreed.

The campaign of pressure against Iran began in earnest in the 2005-2007 period, when the U.S. adopted authorities to impose sanctions on WMD proliferators. In 2007 the U.S. designated Iranian state-owned Bank Sepah for facilitating the procurement of material needed for missiles capable of carrying weapons of mass destruction.⁶ Later that year, the Treasury Department designated the Islamic Revolutionary Guard Corps (IRGC), Banks Melli and Mellat, and several other entities for involvement in Iran’s WMD and ballistic missile programs.⁷

The U.S. strategy to impose pressure on Iran over its WMD program accelerated substantially in 2010 with the Comprehensive Iran Sanctions Accountability and Divestment Act of 2010 (CISADA), which modified the Iran Sanctions Act and adopted a robust regime of secondary sanctions focused on Iran’s WMD activities and activity of the IRGC. CISADA effectively presented a stark choice to companies around the world—you can do business with designated Iranian entities or do business in the United States, but you cannot do both. CISADA was followed by a number of other legislative and executive measures in subsequent years, such as the FY 2012 National Defense Authorization Act and several others, which made it exceedingly difficult for Iranian entities to function as members of the international commercial system.

The U.S. conducted its sanctions campaign in partnership with others around the world. U.N. Security Council Resolutions starting with UNSCR 1737 in 2006 established an international foundation for the isolation of Iran. And at the same time as the U.S. adopted CISADA, the U.N. Security Council adopted UNSCR 1929, which substantially increased pressure on Iran. In the years since 2005 and especially after 2010, America’s allies and partners banded together to restrict Iran’s access to the international financial system to incentivize it to negotiate regarding its nuclear program. Countries in the EU, as well as others including Japan, Canada, the UAE, and Australia curtailed their dealings with Iran. This was part of a significant coordinated diplomatic effort on the part of the

⁶ “Iran’s Bank Sepah Designated by Treasury Sepah Facilitating Iran’s Weapons Program,” Press Release, U.S. Department of the Treasury, Jan. 9, 2007, <https://www.treasury.gov/press-center/press-releases/Pages/hp219.aspx>.

⁷ “Fact Sheet: Designation of Iranian Entities and Individuals for Proliferation Activities and Support for Terrorism,” Press Release, U.S. Department of the Treasury, Oct. 25, 2007, <https://www.treasury.gov/press-center/press-releases/Pages/hp644.aspx>.

administration and its partners to increase the pressure on Iran, helped significantly by legislation adopted by Congress.

Collaborative efforts with partners were critical to the success of the negotiations that led to the JCPOA, and those partners joined with the United States because they shared the U.S. goal of preventing Iran from obtaining a nuclear weapons program. Now that Iran has committed in the JCPOA to dismantle significant parts of its nuclear program, preserving the JCPOA—the framework in which Iran made those concessions—is an important American interest. Forcing Iran to unilaterally capitulate was never a realistic goal of the sanctions campaign, and sanctions were not imposed for their own sake. The objective was to generate the leverage needed to change Iran’s calculations about its nuclear program, which led to the agreed-upon Joint Comprehensive Plan of Action. Should the U.S. or others depart from their obligations under the JCPOA, Iran will likely feel empowered to do so as well—an outcome that disserves American national interests.

III. Iran’s Commitments Under the JCPOA

The P5+1 and Iran implemented their respective commitments under the JCPOA on January 16, 2016, “Implementation Day.” Most important, Iran committed under the JCPOA that “under no circumstances” will it “ever seek, develop or acquire any nuclear weapons,”⁸ and that with time, Iran’s nuclear program will develop into “a commercial programme for exclusively peaceful purposes, consistent with international nonproliferation norms.”⁹ More specifically, the P5+1 was only obligated to lift certain sanctions imposed on Iran after the International Atomic Energy Agency (IAEA) verified that Iran has fulfilled its nuclear-related commitments. And on Implementation Day, the IAEA certified that Iran did fulfill those commitments, including:

- That Iran rendered calandria in the Arak Heavy Water Research Reactor inoperable by filling openings with concrete such that it will not be usable for a future nuclear application;¹⁰
- That Iran had no more than 130 metric tonnes of nuclear grade heavy water (or equivalent);¹¹
- That Iran had no more than 5,060 IR-1 centrifuges installed at Natanz;
- That Iran was not enriching Uranium above 3.67% at its declared nuclear facilities;
- That Iran had imposed limitations on its centrifuge research and development activities;
- That Iran limited the number of operating centrifuges and other nuclear-related activities at the Fordow Fuel Enrichment Plant;

⁸ Joint Comprehensive Plan of Action at 2, Vienna, Jul. 14, 2015 [hereinafter “JCPOA”].

⁹ *Id.*

¹⁰ *Id.* at Annex I, B.3

¹¹ Report by the Director General, International Atomic Energy Agency, *Verification and Monitoring in the Islamic Republic of Iran in light of United Nations Security Council Resolution 2231 (2015)*, IAEA Doc. GOV/INF/2016/1 (Jan. 16, 2016), <https://www.iaea.org/sites/default/files/gov-inf-2016-1.pdf>.

- That Iran had a stockpile of no more than 300 kg of UF₆ enriched up to 3.67% U-235 (or the equivalent in different chemical forms);
- That Iran will apply the Additional Protocol to its Safeguard Agreement;
- That Iran has implemented a range of transparency measures related to the broad scope of its nuclear-related activities; and
- That Iran has committed to facilitating a long-term IAEA monitoring presence in supervision of its nuclear program.

Since Implementation Day, the Director General of the IAEA has issued two quarterly reports to the IAEA's Board of Governors on its activities to verify and monitor Iran's compliance with the JCPOA, the latest of which was submitted on May 27, 2016.¹² The reports raised no concerns about Iran's compliance with the JCPOA. Approximately six months after Implementation Day, there is therefore no evidence that Iran has materially breached the agreement.

IV. U.S. Sanctions After the JCPOA

In exchange for Iran's concessions on its nuclear program the P5+1 agreed to lift or modify a number of its sanctions on Iran. These include significant portions of the EU's Iran sanctions regime as well as the bulk of the U.N.'s Iran sanctions program. Many of the most important changes, however, are those that occurred to the U.S. sanctions regime. In the JCPOA, the U.S. committed to lift nuclear-related secondary sanctions on Iran, which constitute most of the secondary sanctions it has on Iran, while it retained (with a few exceptions) its primary sanctions program.

Secondary sanctions are those that apply to foreign individuals and entities that may have U.S. business relationships, but are not otherwise subject to U.S. jurisdiction. The secondary sanctions that were eliminated would have imposed consequences on foreign companies that engaged in banking, insurance, or a range of other types of relationships with Iranian entities linked to proliferation prior to the JCPOA. The goal of relaxing sanctions in this way was to facilitate the ability of non-U.S. companies, including non-U.S. banks, to re-engage with Iran. In exchange for this relief, Iran agreed to the significant limitations on its nuclear program described above. These limitations make a critical contribution to the global security environment by ensuring that if Iran adheres to the terms of the deal, it will take at least one year from a decision to build a nuclear weapon for it to "break out" to produce enough weapon-usable material for use in a device. While nuclear-related secondary sanctions were suspended as a result of the JCPOA, some secondary sanctions do remain, including those that could be used to target foreign entities doing business with the IRGC or other Iranian individuals or entities on OFAC's Specially Designated Nationals (SDN) list.

But despite the many secondary sanctions on Iran that were lifted, most primary U.S. sanctions remain, with broad reach. Primary sanctions are those that apply to individuals

¹² Report by the Director General, International Atomic Energy Agency, *Verification and Monitoring in the Islamic Republic of Iran in light of United Nations Security Council Resolution 2231 (2015)*, IAEA Doc. GOV/2016/23 (May 27, 2016), <https://www.iaea.org/sites/default/files/16/06/gov2016-23.pdf>.

and entities subject to U.S. jurisdiction, and the U.S. primary sanctions on Iran, including a near-comprehensive trade embargo, remain the strictest in the world even after the JCPOA. A common way in which U.S. jurisdiction is triggered is when U.S. Dollar-denominated transactions clear through the U.S. financial system. That almost all significant U.S. Dollar-denominated transactions anywhere in the world clear through the United States means that anyone conducting those transactions (including, for example, to purchase Iranian oil) is subject to U.S. sanctions.¹³ Even for those who are not legally bound by U.S. sanctions, the size and importance of the U.S. financial system, and the reputational risk involved in doing business with Iran, means that banks and companies around the world often adhere to U.S. sanctions even if they are not obligated to do so.¹⁴ The U.S. sets the tone for sanctions compliance and enforcement globally.

Although the U.S. primary sanctions regime generally bars persons subject to U.S. jurisdiction from doing business with Iran, the JCPOA included three main exceptions to that general rule (there have long been exceptions to sanctions against Iran for the provision of humanitarian goods, among others). These three exceptions entailed the creation of licensing mechanisms so that: 1) U.S. persons can import Iranian-origin carpets and foodstuffs;¹⁵ 2) U.S.-owned or -controlled foreign entities can engage in certain transactions with Iranian individuals or entities (with some limitations); and 3) U.S. persons with a license may sell commercial passenger aircraft and related parts and services to Iran, but the licenses issued “will include appropriate conditions to ensure that licensed activities do not involve ... any person on the SDN list.”¹⁶

This is the provision of the JCPOA that would allow Boeing and Airbus to sell aircraft, and aircraft parts and maintenance services to Iran, many of which will be used to ensure the airworthiness of Iranian planes—a humanitarian goal in its own right insofar as it protects the ability of ordinary Iranians to travel safely. In considering the appropriateness of any agreement to sell aircraft to Iran for commercial use, it is important to focus on conditions designed to ensure that those sales don’t involve prohibited parties.

V. Continuing Challenges with Respect to Iran

As we can see, therefore, the strategic relationship and financial landscape with respect to Iran remain complex. Strategically, Iran’s support for terrorism, the regime of Bashar al-Assad in Syria, and groups that destabilize a range of U.S. allies and partners in the Middle East, mean that Iran remains an adversary of the United States. With respect to

¹³ Shortly after Implementation Day, Iran attempted to denominate oil transactions in Euros, which would minimize the likelihood the transactions would be subject to U.S. jurisdiction. Nidhi Verma, *Exclusive: Iran Wants Euro Payment for New and Outstanding Oil Sales*—Source, REUTERS, Feb. 8, 2016, <http://www.reuters.com/article/us-oil-iran-exclusive-idUSKCN0VE21S>.

¹⁴ The most common ways to trigger a jurisdictional link to the United States include the involvement of U.S. citizens or lawful permanent residents in transactions, the involvement of companies organized under the laws of the United States or any state, the involvement of people physically inside the United States, or clearing U.S. Dollar-denominated transactions through the U.S.

¹⁵ Iranian Transactions and Sanctions Regulations, 31 CFR § 560.534.

¹⁶ JCPOA Annex II at §5.1.1 n. 12.

the commercial landscape, the P5+1 provided Iran relief from nuclear-related sanctions in exchange for significant constraints on its nuclear program. But global enterprises rightly remain wary of conducting business in Iran. This is because U.S. sanctions on Iran were only partially lifted, because Iran has not developed a meaningful anti-money laundering and counter-terrorist financing (AML/CFT) regime, because of Iran's history of corruption, and because of concerns about the soundness of its banking system, among many others.

There are several specific financial sector risks involved in doing business in Iran, including risks associated with its ongoing support for terrorism. Despite recent government actions that suggest a revised approach to corruption,¹⁷ Iran's record on this issue will continue to make foreign businesses wary. The Financial Action Task Force (FATF), the global AML/CFT standard-setting body, recently retained its identification of Iran's strategic deficiencies in AML/CFT regulation, but suspended its call for countermeasures against Iran in light of Iran's adoption of a strategic plan to address failings in its financial regulatory system.¹⁸ While this measure recognizes Iran's high-level political commitment to improving some problems in its financial system, it has not undertaken enough change to provide the assurance that international investors need to commit to major deals with Iran. The opacity that characterizes much of the Iranian economic and political system makes it very challenging to do business there with confidence that foreign companies can avoid transactions with prohibited parties.

This is a particular risk with respect to the IRGC, which controls large portions of the Iranian economy in ways that might not always be obvious, and against whom U.S. secondary sanctions remain in place. Entities choosing to do business in Iran must be confident that they are not engaging in prohibited transactions with the IRGC or other still-designated entities, but achieving that level of assurance will be very difficult.

They must also guard against the risk that goods or services provided to Iran under the terms of the JCPOA, including aircraft, are diverted from permissible commercial purposes to nefarious ends. There is always a chance that this will take place. And that is why it is important to establish the kinds of conditions and monitoring and verification procedures that will allow companies to proceed with JCPOA-compliant business with as much confidence as possible. This requires effective due diligence, creative contractual terms and licensing conditions, ongoing monitoring, and a collaborative relationship between government and private sector. It is also incumbent on the U.S. Government to monitor the situation closely to ensure that any diversion from legitimate ends is detected in a timely manner and that appropriate enforcement actions are taken.

The mixed record of international commercial engagement with Iran since Implementation Day reflects the challenges involved. After the JCPOA was signed in 2015 there was some initial enthusiasm about re-engaging with Iran. During the first half

¹⁷ Shirzad Bozorgmehr and Joshua Berlinger, *Iranian Billionaire Sentenced to Death*, CNN, Mar. 8, 2016, <http://www.cnn.com/2016/03/06/middleeast/babak-zanjani-death-sentence/>.

¹⁸ Public Statement, Financial Action Task Force (June 24, 2016), <http://www.fatf-gafi.org/publications/high-riskandnon-cooperativejurisdictions/documents/public-statement-june-2016.html>.

of 2016, for example, there were reciprocal visits between the President of Iran and Prime Minister of Italy, during which a number of commercial deals were reportedly signed.¹⁹ But there has also been reluctance on the part of the international commercial community, particularly among the large global banks, to re-engage.²⁰ They are wary of residual sanctions, a difficult commercial climate, and the reputational risks entailed with doing business in a country that engages in widespread human rights abuses and support for terrorism.²¹ Indeed, the U.S. government's finding that Iran is a jurisdiction of primary money laundering concern remains on the books. In light of this situation, reports about the business that has taken place suggest that it is facilitated by smaller European or Turkish banks that have limited connectivity to the U.S. financial system.²²

VI. Conclusion: A Path Forward

The protection of American interests in the Middle East depends on our ability to pursue two paths simultaneously with respect to Iran. First, as long as Iran maintains the integrity and viability of the JCPOA, the P5+1 must do so as well. The JCPOA put meaningful agreed-upon limits on Iran's nuclear program for the first time. Without such limits, Iran would be constrained only by its ability to obtain the inputs needed for a nuclear weapons program, and could be checked only by the willingness of the international community to take extreme measures to stop it. The JCPOA therefore serves a significant American strategic interest by binding Iran to a framework limiting its nuclear program to which Iran itself agreed. We should do what we can to ensure that the JCPOA continues to serve that function, and for the sake of American credibility as well as the viability of the deal, should not stand in the way of Iran obtaining the relief to which the P5+1 committed in the JCPOA.

The U.S. has fulfilled its end of the bargain by lifting nuclear-related secondary sanctions, and establishing the licensing regimes needed for U.S. persons to sell aircraft and related parts and services to Iran, to purchase Iranian foodstuffs and carpets, and to allow foreign subsidiaries of U.S. companies to do business there in certain circumstances. While it is undoubtedly risky for companies to engage in this kind of business, it is clearly permitted by the JCPOA.

With respect to permissible Iran-linked business there is an important role for the government and the private sector to play in monitoring that activity to ensure it stays within the bounds established by the JCPOA. Congress is very well-suited to perform this oversight function—to monitor, to hold hearings, to request information, and to

¹⁹ Nasser Karimi, *Iran and Italy Sign Several Deals During Visit by PM Renzi*, THE ASSOCIATED PRESS, Apr. 12, 2016, <http://bigstory.ap.org/article/0a37f20a0a0045dd9ca74196456d68cf/iran-and-italy-sign-several-deals-during-visit-pm-renzi>.

²⁰ Carol Morello, *Asian and European Banks are Still Shunning Iran—And Tehran Blames the U.S.*, WASH. POST, May 10, 2016, https://www.washingtonpost.com/world/national-security/asian-and-european-banks-are-still-shunning-iran--and-tehran-blames-the-us/2016/05/10/82a5a2c4-138e-11e6-8967-7ac733c56f12_story.html?tid=a_inl.

²¹ Stuart A. Levey, *A Peculiar Message About Iran for European Banks*, WALL ST. J., May 12, 2016, <http://www.wsj.com/articles/kerrys-peculiar-message-about-iran-for-european-banks-1463093348>

²² Benoit Faucon, *Iran's Oil Deals Hit Banking Snag*, WALL ST. J., May 26, 2016.

ensure that all parties to the JCPOA scrupulously adhere to its terms. This goes for Iran, in the conduct of those nuclear activities that the agreement allows it to retain, and for those companies that choose to re-engage in permissible Iran-linked business. Ultimately whether companies choose to do business in Iran is a commercial decision that each will make on its own terms.

Second, the United States and its allies and partners must continue to maintain pressure on Iran so that it changes the behavior that is inimical to U.S. interests—its support for terrorism, repressive regimes, and human rights abuses inside Iran and outside of it. The U.S. and its allies retain a wide range of tools with which to do this, including all of the traditional tools of statecraft—coercive diplomacy, sanctions, and military and diplomatic alliances. The U.S. in particular retains the ability to impose extremely powerful non-nuclear secondary sanctions on parties that engage in business activities with Iranian SDNs, among others.

The challenge for the government and the private sector, for the administration and for Congress, is great. All must work together to ensure the integrity and viability of the JCPOA as an effective mechanism for constraining Iran's nuclear ambitions. But all must work together, too, to use all available means to protect American interests and to limit Iran's malign influence throughout the Middle East and the world.