

U.S. Oil Company

A STRATEGY TO PERSUADE THE U.S GOVERNMENT TO SUPPORT THE CONSTRUCTION OF AN OIL AND GAS PIPELINE THROUGH IRAN

ADDRESSING CURRENT U.S. ECONOMIC SANCTIONS AGAINST IRAN

By DANA BAIKENOVA
M.A. PROJECT

ADVISOR: ANDREW PROCASSINI

MONTEREY INSTITUTE OF INTERNATIONAL STUDIES

This paper was researched and written to fulfill the M.A. project requirement for completing the Monterey Institute of International Studies' Master of Arts in Commercial Diplomacy. It was not commissioned by any government or other organization. The views and analysis presented are those of the student alone. For more information about the Commercial Diplomacy program and the M.A. project requirement, please visit www.commercialdiplomacy.org.

Table of Contents

- I. [Scenario](#)
- II. [Executive Summary](#)
- III. [Background](#)
- IV. [Analysis of Substantive Issues](#)
 - 1. [Commercial Issues](#)
 - 2. [Policy Issues](#)
 - 3. [Environmental Issues](#)
 - 4. [U.S. Unilateral Sanctions](#)
 - 5. [U.S. Domestic Political Issues](#)
- V. [Comprehensive Strategy](#)
 - 1. [Domestic Strategy](#)
 - a) [Coalition Building](#)
 - b) [Legislative Strategy](#)
 - c) [Media Strategy](#)
 - d) [Business to Government Negotiation Strategy](#)
 - 2. [International Strategy](#)
 - 3. [U.S. -Iran Bilateral Strategy](#)
- VI. Appendices
 - A. [Export Pipeline Routes](#)

- B. [Caspian Sea Region Oil Production & Exports](#)
 - C. [Oil & Gas Reserves in the Caspian Region](#)
 - D. [Oil Routes in the Caspian Region](#)
 - E. [White Paper](#)
 - F. [Congressional Testimony](#)
 - G. [Letter to Coalition Member](#)
-

SCENARIO

For the purpose of this project, I assume the fictitious role of vice president of government and international affairs of a fictitious company, U.S. Oil Company.

U.S. Oil Company has invested in several oil and gas projects in the Caspian region. It has a strong vested interest in the development of a pipeline that will transport Caspian oil and gas to world markets by the most efficient means possible. In U.S. Oil's view, the best option is to construct a pipeline through Iran to the Persian Gulf. However, U.S. policy prohibits American companies from doing business in Iran. Accordingly, I have been tasked to design a strategy to persuade the United States government to alter its policy and allow U.S. Oil to take part in the construction of a pipeline through Iran.

The strategy is designed to capitalize on the fact that the United States and Iran are already beginning to move towards the mutual realization that change and reform in their relationship is becoming increasingly necessary, especially for strategic purposes in the Caspian Sea region.

EXECUTIVE SUMMARY

A Strategy to persuade the U.S Government to recognize the Iranian pipeline as the best option for transporting Caspian oil and gas to world markets.

Issue

U.S. Oil Company wants to participate in the construction of an oil and gas pipeline through Iran. However, because of the United States' unilateral economic sanctions against Iran (the Iran-Libya Sanctions Act of 1996, or ILSA), U.S. Oil is prohibited from participating in the construction of the Iranian pipeline.

Objectives

U.S. Oil's primary objective is to convince the U.S. government to support the construction of a pipeline through Iran and to modify ILSA to allow companies to participate in the pipeline project. U.S. Oil's long-term goal is to convince the U.S. government to lift the sanctions against Iran.

Background

The Caspian region is believed to hold about 100-200 billion barrels of crude oil, and it holds natural gas potential as well. The successful development of this rich region depends upon a number of issues including transportation issues, legal issues concerning national property rights, the region's political stability, energy security issues, environmental concerns, financial issues, and the United States' unilateral sanctions against Iran.

The Caspian region currently lacks export pipeline capacity. U.S. Oil and others hope to build multiple pipelines in order to facilitate the export of energy resources to diverse world markets. U.S. Oil is particularly concerned with building pipelines that are both commercially viable and environmentally safe.

At least nine to ten pipelines have been proposed, and some are already under construction. All have advantages and disadvantages. Some pipelines require huge investment, some pass through politically unstable territories, and others are environmentally risky.

The Iranian option is the safest and most economical route currently available. It is the cheapest route; it requires the shortest lead-time for construction; it avoids politically unstable regions; and it poses almost no environmental risk. In addition, a pipeline through Iran is desirable because transporting oil to the Persian Gulf rather than the Mediterranean will facilitate the transport of Caspian energy resources to Asian markets where demand is expected to grow in the coming years.

Investing in an Iranian pipeline rather than an alternative option will allow U.S. Oil to transport its oil more economically and will save the company millions of dollars. The Iranian pipeline option offers lower tariffs and the highest return on investment.

The United States should not ignore the Iranian route. The pipeline through Iran is the most logical, economical and commercially viable option, as well as one of the most environmentally sound. Moreover, the Iranian regime recently began moderating some of its positions and practices, which makes it possible to envision a potential limited waiver of the ILSA rules for U.S. oil projects.

Strategy Proposal

U.S. Oil's strategy includes both domestic and international action plans for persuading the U.S. government to support the Iranian pipeline option and, in the long run, to change its policies towards Iran.

Domestic strategy

- **Coalition Building Strategy.** A Coalition for Caspian Energy Development (CCED) will be established to generate broad U.S. support for the successful development of the Caspian region (including reform of the United States' unilateral sanctions). CCED will include major American oil companies that are already invested in the Caspian region. Trade and industry associations will also be included.
- **Legislative Strategy.** This strategy calls for direct lobbying of members of the U.S. Congress. It's goal is a repeal, or at least a waiver of, ILSA.

- **Media Strategy.** The media will be used to create greater visibility of issues involved in Caspian region development. The strategy's goal is to generate sufficient support from decision-makers in Washington, DC. It will emphasize the recent positive signs from the Iranian president and the strategic importance of Iran in Caspian region development. A second emphasis will be on the importance of international trade and the impact of unilateral sanctions on the U.S. economy-impacts including lost business opportunities and jobs and lost U.S. competitiveness in the Caspian region.
- **Negotiation Strategy.** The negotiation strategy relies on business-to-government negotiations.

International Strategy

The international strategy involves creating international pressure to push the United States to reform its policies toward Iran. To accomplish this goal, an international coalition will be formed with membership that includes representatives from regional governments, the business community (including foreign oil and gas companies), NGOs, and regional U.S. Chambers of Commerce.

- **Coalition Building Strategy.** The objective of an International Coalition for Caspian Region Economic Development (ICCRED) is to build international support and consensus for changes in U.S. policy. The International Coalition will initiate the same action plan as the domestic coalition but on the international level.
- **Media Strategy.** This strategy is designed to heighten the public's and policymakers' awareness of the importance of Iran to the development of the Caspian region and to highlight Iran's recent positive signals to the United States. The media campaign should also focus on the advantages of building a pipeline through Iran and on the negative impact of the U.S. unilateral sanctions against Iran.
- **U.S.-Iran Bilateral Negotiation Strategy.** The negotiation strategy provides recommendations for how best to approach negotiations between the United States and Iran.

BACKGROUND

The Caspian Region

The collapse of the Soviet Union in 1991, along with the emergence of independent states in the Central Asian and Caucasus regions, has reopened the vast resources of the Caspian Sea to development. The Caspian Sea region is believed to hold up to 200 billion barrels of recoverable energy reserves. Kazakhstan has the largest oil and gas reserves with almost 40 percent of the region's potential, Azerbaijan is estimated to hold about 25 percent, and Turkmenistan holds as much as 15-20 percent. Russia holds only about six percent.

The Caspian Basin region consists of five littoral states: Azerbaijan, Iran, Kazakhstan, Russia, and Turkmenistan. It is 700 miles long, contains six separate hydrocarbon basins and is considered to be a second "North Sea" in terms of its energy resources potential. Since the region has not yet been developed, it has become the focal point for foreign oil company investment. The region has been a source of great expectation and opportunity, as well as controversy.

Most of the oil and gas reserves in the Caspian region have not been developed and much of the region remains unexplored. Most of Azerbaijan's oil resources are located offshore, along with approximately 30 to 40 percent of Kazakhstan's and Turkmenistan's total oil resources. Proven oil reserves for the entire Caspian Sea region are estimated at 16 to 32 billion barrels, compared to 22 billion barrels in the United States and 17 billion barrels in the North Sea. Natural gas reserves are even larger, accounting for almost two-thirds of the hydrocarbon reserves in the region. Based upon proven reserves, Kazakhstan, Turkmenistan and Uzbekistan each rank among the 20 countries with the largest natural gas resources.

A number of issues will need to be addressed before the region's vast energy potential can be fully developed. Key issues include:

- Property rights-legal issues between the littoral states concerning ownership and development rights in the Caspian Sea.
- Regional instability.
- Energy security.
- Transportation/pipeline issues-the need to develop transnational export routes to take oil and gas from the landlocked Caspian Sea region to world markets.
- Finance and investment.
- U.S. unilateral sanctions against Iran.
- Iran's strategic role in the region.

The Caspian region has become the leading area for investment in the former Soviet Union. In the energy sector alone, approximately \$3 billion will be invested by the end of the year. In the process, Caspian governments and private investor groups from the United States, the United Kingdom, Russia, Turkey, France, Italy, Norway, Holland, Canada, Indonesia, China, Saudi Arabia, Argentina, Malaysia, and South Korea now have a shared interest in the rapid development of Caspian energy reserves. The strengthening of independent, stable states in the Caspian region is a necessary basis for long-term energy development.

Investment in Kazakhstan's oil and gas industries already totals \$2 billion and is expected to continue in the future. Indeed, an agreement has been signed that will bring in an additional \$600 billion over the next 40 years.

Established joint ventures and consortiums in the region

A large number of oil and gas-related joint ventures have been established in the Caspian region during the past five years. The largest ventures established to date include the following:

Azerbaijan -

- The Azerbaijan International Operating Company (AIOC), which is further developing the Azeri-Chirag-Guneshli project.

- The Caspian International Petroleum Company (CIPCO), which is developing the Karabach project.
- The Shahdeniz project, which is the most recent and led by BP.
- The DanUlduzu project led by Amoco, with overall estimated investments in excess of \$20 billion and expected production levels well above one million barrels per day by 2010.

Kazakhstan -

- The Caspian Pipeline Consortium (CPC). Members include: Russia (24 percent), Kazakhstan (19 percent), Chevron (15 percent), LukArco (12.5 percent-Russia/USA), Mobil (7.5 percent), Rosneft-Shell (7.5 percent-Russia/UK/Netherlands), Oman (7 percent), BG (2 percent-UK), Agip (2 percent-Italy), Kazakhstan Pipeline Ventures (1.75 percent), and Oryx - 1.75 percent.
- The onshore Tengizchevroil Joint Venture. Members include: Chevron (45percent), Mobil (25 percent), Kazakhstan (25 percent), and LukOil (5 percent). This venture is already producing 160,000 barrels of oil per day. It is expected to raise \$20 billion in investment and reach a production level of more than 700,000 barrels per day before 2010.
- The Caspian Sea Consortium (CSC) consists of Agip, BP/Statoil, British Gas, Mobil, Royal Dutch/Shell and Total.

Transportation/Pipeline Issue

The lack of pipeline capacity represents the key constraint to energy development in the Caspian region. Because the Caspian Sea is landlocked, pipelines are crucial for transporting oil and gas reserves to world markets. Moreover, because the region's existing pipelines were designed to link the Soviet Union internally, they are routed through Russia. Although some of Russia's pipelines are underutilized, they do not have the capacity to absorb all of the oil and gas the region can produce, and other countries do not want to be reliant on Russia for their oil export revenues. It is clear that new pipelines are needed.

Export Routes

Each of the proposed pipeline routes has certain disadvantages. Some are very costly to build and operate while others pose serious environmental hazards. Most pass through politically unstable regions. The Iranian option is the least hazardous and most economical. Each pipeline route is outlined below.

"Western Route"

Azerbaijan, Georgia, Turkey and the United States favor this route. The western oil route for early oil from the AIOC would pass from Baku, Azerbaijan to the Georgian port of Supsa on the Black Sea. This pipeline is expected to become operational by April 1999. The route from Baku to Supsa is considered one of the better options for the Main Export Pipeline (MEP).

This pipeline is economically viable and, more importantly, does not require large capital investments at the beginning stage of the project. This route also requires minimal transportation costs and tariffs. However it passes through politically unstable regions

and, because oil would ultimately be shipped from the Black Sea via the Bosphorus Straits, it presents a potential environmental danger.

- Cost: \$1 to 1.5 billion.
- Political Instability: This route would pass through Russia, the Caucasus region and finally to the Georgian port of Supsa. Although there are no major security problems in Russia, the Georgian region is still somewhat unstable due to its recent war with Abkhazia.
- Environment: In order for oil to get from Supsa to world markets, it needs to be transported by tankers through the narrow, difficult to navigate Bosphorus Straits. The route cuts through the densely populated sprawl of Istanbul and would create an additional burden to the already heavy traffic on the Bosphorus. If anything were to go wrong, it would result in environmental disaster.

"Northern Route"

This pipeline would carry oil from Baku, Azerbaijan, across Chechnya, through Russia and to the Black Sea port of Novorossiisk. This route has problems similar to those of the Western Route.

- Cost: \$2.4 billion to repair the Chechen line (section that passes through Chechnya).
- Political Instability: This route passes through a very unstable region in Chechnya, which puts the security of the oil in question. Construction has already been delayed due to postponed negotiations between the Russian and Chechen authorities.
- Environment: This route also takes oil to the Black Sea and through the Bosphorous Straits.

"Mediterranean Route"

This pipeline would begin in Baku and cross Turkey to the Mediterranean port of Ceyhan. It is one of several being considered for the Main Export Pipeline (MEP) for oil from Azerbaijan, and the governments of Azerbaijan, Georgia, Kazakhstan, Turkey, and Uzbekistan have already signed the Ankara declaration on construction of the MEP to Ceyhan (with Turkmenistan abstaining). Washington and Turkey also support the route.

This route is one of the longest and most expensive of all the options, and many players remain unconvinced that the line would be economically viable. Indeed, members of the AIOC have delayed choosing a route and companies have delayed financing this pipeline because of the pipeline's high cost of construction, the high tariffs demanded by Turkey for transit on its territory, and the lack of a guaranteed oil volume to make such a huge pipeline worthwhile. The current low price of oil has only added to concerns about the route's profitability.

If Kazakh crude volume is added to Azerbaijani crude, it would make more commercial sense to build this pipeline, and it has been suggested that Kazak oil could be shipped to Baku and transported via this line. As discussed below, a Trans-Caspian pipeline project, which is also being considered, would facilitate transport of Kazak oil to Baku.

- Cost: \$2.3 to 3.5 billion for a pipeline from Baku to Ceyhan; \$3.6 to 4.2 billion for a pipeline from Kazakhstan to Baku and then to Ceyhan (by far the most expensive of all proposed pipeline routes).

- Political Instability: The pipeline would have to pass near Kurdistan and areas in which Turkey has carried out a bitter and costly military conflict with its Kurdish population. It is questionable whether this pipeline would benefit or harm the interests of Kurds.
- Environment: This option is more environmentally friendly since the Bosphorus is bypassed- although a Trans-Caspian line presents environmental concerns.
- Other factors: There is currently no agreement from oil companies to finance this route and not enough oil volume to fill such a large pipeline.

Trans-Caspian Pipeline Project

The Trans-Caspian project of the "Eurasian corridor" is controversial primarily because the pipeline would be underwater and therefore poses a significant risk to the environment and the Caspian's bio-resources. Additionally, building this pipeline will require the resolution of property rights issues in the Caspian (i.e., which countries have what resource development rights).

Azerbaijan is extremely interested in this project because it would bring great profits and political dividends to the country. The United States is interested because the additional oil from Kazakhstan will help justify the expense of the Baku-Ceyhan pipeline. Kazakhstan is interested because it would facilitate the export of its oil reserves. Russia and Iran strongly oppose the project because of the risk it poses to the environment and its bio-resources.

High construction costs are also a concern. In order to cover the cost of construction, all oil from western Kazakhstan would need to be transported via this pipeline.

- Cost: \$3.5 to 4.2 billion
- Political instability: The pipeline would pass through the Caucasus region and areas of Georgia that still have problematic political situations.
- Environment: Since part of the pipeline from Kazakhstan to Baku will be built underwater, it presents a significant environmental threat. For now, however, the plan is to ship Kazakh crude to the port of Baku, then transport it by pipeline to Ceyhan.

CPC Pipeline

The Caspian Pipeline Consortium (CPC) has already begun construction of a 1.34 million-bb/d oil export pipeline that will bring Tengiz oil to the Russian Black Sea port of Novorosiisk. The CPC will renew an existing pipeline from Tengiz to the Astrakhan region, as well as build a new pipeline from the Astrakhan region to Novorosiisk. The pipeline is expected to be operational in mid-2001 but will not reach its full capacity until sometime in the following decade. It was estimated that during its 35- to 40-year expected life, this pipeline will bring in \$33 billion in revenues for the Russian government, including \$23 billion in taxes. Kazakhstan's tax revenues are projected to be \$8 billion.

This route makes Kazakhstan dependent on Russia, and Kazakhstan's economic interests do not altogether coincide with Russian economic interests. Kazakhstan and Russia are competitors on the world hydrocarbon resource market. This route is also questionable

because of the war in Chechnya, and exporting from Novorosiisk does not guarantee that Kazakh oil will reach Europe due to the problem of "low transit capacity."

- Cost: \$2.2 billion.
- Political Instability: The war in Chechnya.
- Environment: This route requires transporting oil through the Bosphorus Straits.

"Eastern Route" (To China)

Building a pipeline through China will cost much more than any other pipeline because such a line would be much longer than any other. However, Kazakhstan and China have already signed a deal, and despite the high cost, the Chinese will most likely build the line for strategic reasons.

The line would include the world's largest natural gas pipeline (2000km), stretching from Turkmenistan and Kazakhstan to the Chinese coast, and it would potentially continue to Japan. Exxon, Mitsubishi, and China National Petroleum have already submitted a preliminary feasibility study for the construction of this pipeline. A feasibility study for an oil pipeline from Kazakhstan and Turkmenistan to China is expected to be completed in 1999.

Both pipelines face numerous financial and technical difficulties due to the length of the route, as well as the terrain it traverses. The oil line would need to be 8000km long and would cost around \$9 billion.

Taking into account that by the year 2010 China could be among the biggest consumers of oil, this route could be one of the highest priority projects for Kazakhstan.

"Southern Route" (Via Iran to the Persian Gulf)

This route would traverse Iran to the Persian Gulf; it is the most commercially and economically viable route. Iran already has a pipeline system, and the Gulf is a very good export point for serving Asian markets. Although American oil companies support this route, the U.S. government strongly opposes it. Because of the United States' unilateral economic sanctions against Iran, American companies are prohibited from engaging in any business activities with Iran.

- Cost: \$1.5 to 2.5 billion.
- Political Instability: Although the United States views Iran as a threat, the country is far more stable than the regions through which other pipeline options pass.
- Environment: No significant risk in comparison to other options.
- Other factors: The Iran-Libya Sanctions Act (ILSA) prohibits U.S. companies from investing in Iran.

The best export route for oil from Kazakhstan and Turkmenistan is directly south, through Iran, via a proposed new pipeline to Tehran and Iran's network of pipelines and refineries. There are two other options for transporting oil from Azerbaijan to the Persian

Gulf: 1) ship the oil east from Baku across the Caspian Sea to the port of Turkmenbashi, Turkmenistan, where it could connect with the proposed new pipeline; or 2) transport the oil from Baku via a proposed 190-mile pipeline to Tabriz in northwest Iran where it would also connect with the existing Iranian pipeline network.

"Southeastern route" (To Pakistan via Afghanistan)

A pipeline is planned to go through Afghanistan to Pakistan and possibly on to India. The estimated cost is \$1.9 billion for each section. Geographically this route is feasible; however, the ongoing war in Afghanistan has prevented the project from moving forward.³ No progress has been made on this pipeline.

Country Positions on Export Pipelines and Investment in Iran

Position of the United States Government

The United States supports the construction of multiple pipelines in order to ensure that no one country can monopolize the delivery of Caspian energy resources to world markets. The United States' route preferences follow:

- The United States supports an east-west pipeline through its ally, Turkey. This route is very controversial, however. Even though the declaration to build this pipeline was signed, the decision and actual financing for it has been postponed due to the many questions and doubts regarding its economical and commercial viability. The AIOC has not yet decided on this one million bb/d pipeline as its Main Export Pipeline (MEP).
- The United States supports the involvement of Russia in development of Caspian resources. However, the United States would like to avoid the Russian route as a main pipeline option.
- The United States strongly opposes the conduct of business with Iran.

Position of the Kazakhstan Government

The government of Kazakhstan is looking for routes that offer the best balance between low transportation costs and sales in high value markets. The government of Kazakhstan sees the southern route, via Iran, as logical and economically viable. Crude values are higher via this route, transit costs are much lower, and Kazakhstan has overall good, long-standing relations with Iran. However, Kazakhstan faces a dilemma in that the largest part of foreign direct investment in Kazakhstan and the region comes from the United States. The majority of investors, stakeholders and shareholders in the region are American firms. Thus, Kazakhstan finds itself in a difficult situation. It would like to support, build and operate an Iranian pipeline, but it doesn't want to risk its relationship with the United States and U.S. businesses.

Position of the Turkmenistan, Azerbaijan and Russian Governments

The countries in the Caspian region aim to diversify their export routes as much as possible. However, Turkmenistan, Azerbaijan and Russia consider the Iranian option very promising; none of these countries have problems with Iran. Despite the U.S imposed sanctions, many Caspian states have already engaged in, and profited from,

business and trade activities with Iran. They would like to invest in an Iranian-route pipeline and engage in swapping arrangements with Iran. The following are examples of projects that are developing with Iran:

- Azerbaijan - Azerbaijan's SOCAR and National Iranian Drilling Company (NIOC) formed a joint venture to conduct seismic surveys and drill exploratory wells in the Iranian sector of the Caspian Sea.
- Kazakhstan - Iran and Kazakhstan agreed to a swapping arrangement for Kazakhstan's crude exports.
- Turkmenistan - There is one gas pipeline that is already under construction that will go from Turkmenistan to Iran.

European Investment Activities in Iran

The U.S Administration recently waived sanctions for foreign firms doing business in Iran. As a result of the waiver, European oil and gas companies are getting involved in big, profitable projects in Iran:

- Following the cancellation of the Conoco deal, the French firm Total SA reached an agreement with Iran for development of the Sirri A and E fields.
- In June 1996 a Malaysian firm, Petronas, acquired a 30 percent stake in the project.
- Following the passage of ILSA, Iran and Turkey signed a 22-year gas supply deal worth an estimated \$20 billion.

Iran

Iran is a key player in the Gulf region. It is OPEC's second largest oil producer and accounts for about five to ten percent of global oil output. Iran holds nine percent of the world's oil reserves and 15 percent of its gas reserves. However, Iran remains a focal point for regional security issues.

History of U.S. - Iran Relations

The U.S government has been involved in Iranian politics since about 1953 when Iran's constitutional government was overthrown. Iranians blame Americans for the power the monarchy held for the subsequent 25 years. The 1979 revolution was very anti-American, and the resulting hostage situation at the U.S. embassy created a major crisis in U.S.-Iranian relations. In 1984, the United States placed Iran on the list of states that support international terrorism, triggering statutory sanctions that prohibit weapons sales and require the United States to oppose all loans to Iran from international financial institutions. In 1987, the U.S. further prohibited the importation of any goods or services from Iran, and U.S. naval and air forces struck Iranian naval units on several occasions in response to Iranian efforts to disrupt the flow of oil from the Persian Gulf.

In 1995, President Clinton imposed comprehensive sanctions on Iran, prohibiting all U.S. companies and their foreign subsidiaries of conducting commercial and financial transactions with Iran.

Iran - Libya Sanctions Act (ILSA)

For almost 20 years, the United States has tried to influence Iran by imposing tough economic sanctions against the country. This policy worked as long as the international community supported sanctions. However this is no longer the case.

In August 1996, President Clinton signed the Iran and Libya Sanctions Act (ILSA), which requires the President to impose sanctions against foreign companies that invest \$40 million during any one-year period for development of Iranian or Libyan petroleum resources. One year later, the maximum allowable investment was dropped to \$20 million. ILSA requires that sanctions be imposed for a minimum of 2 years. The sanctions under ILSA, as well as other executive orders, also apply to any joint-use arrangements in the Caspian Sea. The President may waive imposition of the sanctions if he determines that it would be in the national interest of the United States.

Recent Developments in Iran

The democratic election of President Khatami in 1997 was a major positive development for Iran. Khatami was elected largely on a platform of social justice, and he is making efforts toward economic and political reforms. To gain needed capital, he is also trying to make Iran more attractive for foreign investment, especially in the oil and gas sector.

Since 1997, Iran has made substantial progress in improving relations with several countries, and Khatami is taking steps towards moving the country in the direction of better diplomatic, business, economic, and political relations with other countries. The new president wants to end the isolation of Iran and improve the quality of life of the Iranian people. The United States should respond by adopting a policy of engagement towards Iran.

Although significant issues over weapons of mass destruction remain, there is room for normalizing U.S.-Iran relations if the United States makes a positive gesture, such as allowing U.S. companies to invest in the Iranian oil and gas industry.

Analysis of Substantive Issues

The economic development of the Caspian region turns on several issues. The biggest and most important issue is the limited availability of transportation routes for getting oil and natural gas reserves from the landlocked Caspian to world markets. Existing pipelines were built during the Soviet Era, and they are old and unable to handle the large capacity of oil and gas the region can produce. Moreover, they were designed to link the Soviet Union internally, and thus were routed through Russia. While Russia has a commercial and political interest in continuing to be a major transshipment point for Caspian energy resources, Russian routes are not necessarily the most sensible for commercial reasons. Moreover, other countries are reluctant to be reliant on Russia for such a large portion of their income. Indeed, multiple pipelines that take routes through different countries will be necessary so that no country feels that it is totally dependent on another for getting its oil to market.

The pipelines already in place all transport oil to Black Sea ports. The first one runs from Baku to Russia, ending in Novorosiisk. The second, which is being refurbished, stretches from Baku to the Georgian port of Supsa. The third pipeline runs from Kazakhstan to Russia and ends in the Black Sea. All three pipelines have a very limited capacity.

Most of the proposed pipeline routes, including all of those supported by the U.S. government, target the Mediterranean. However, the Mediterranean is already an oversupplied region, whereas demand for energy resources in Asia is increasing. Asian markets are more easily reached by exporting oil through Iran to the Persian Gulf. Moreover, the Iranian route eliminates the need to transport oil through the congested Bosphorus Straits, where the potential for environmental disaster is large, and it eliminates the need to traverse politically unstable regions such as Chechnya, Afghanistan, and Georgia.

Commercial Issues

Iran's existing network of oil and gas pipelines and related infrastructure provide the most logical and lowest cost outlet for Caspian oil resources. It is estimated that 500,000 b/d of pipeline capacity would be available in Iran for transporting oil from north to south. Only minor, connecting pipelines would have to be built over short distances to link existing pipelines to border areas.

Geo-Strategic Arguments for Constructing a Pipeline through Iran

- Iran, apart from Russia, is the only stable country in the region with access to the open sea;
- It shares borders with both Azerbaijan and Turkmenistan;
- It has a large energy infrastructure;
- It has four refineries on Azerbaijan's border; and
- Its export terminal at Kharg Island handles up to 2.5 million bb/d and is capable of handling an even greater capacity.

Economic Arguments

1. The Iranian pipeline offers low transportation costs, low tariffs, and good access to high value markets.
2. The Iranian route requires the shortest lead-time, thus producing revenue faster. Early revenue is worth much more than later revenue, especially if the early route will help in the development of potential future pipelines.
3. The maritime link to Iran is sound. Iran is already an oil-exporter.
4. Iran can modify its northern refineries to take Caspian oil, thus saving the costs of building new refineries.
5. Iran's ability to absorb Caspian oil is also quite large: it could take upwards of 500,000 b/d, and connection would be quick because terminals can be expanded relatively easily.
6. Iranian ports serve consumers in Southeast Asia where demand for energy is predicted to rise substantially over the next decade. In contrast, other options would take crude to the Black Sea and then to European markets, which are already well supplied with oil.

Environmental Arguments

Environmental considerations also make Iranian options more attractive. All the options for routing pipelines to the Black Sea involve shipping oil through the heavily trafficked Bosphorus Straits, where environmental risk is high. The Turkish government has already imposed new restrictions on the use of the Bosphorus because of pollution concerns. The Trans-Caspian pipeline also presents a serious environmental threat. At least two littoral countries, Iran and Russia, will not support this option.

Tradeoffs

Deciding which pipelines to support involves some serious tradeoffs. The quickest and potentially cheapest export route is via Iran. However, the United States strongly opposes any route involving Iran. The less desirable routes involve transporting oil through competitor territories, including Russia and Azerbaijan or through politically unstable territories in Chechnya, Kurdistan and Georgia. These routes are strongly supported by Washington.

In any case, building multiple lines will help make Caspian energy resources more commercially viable and more interesting to private sector oil companies-companies that will finance the bulk of the pipeline projects. There are number of reasons why a diversity of lines is important:

1. Economic reasons: No one nation should be given the opportunity to gain economic dominance over another; all interested parties should benefit from the region's energy resources. These pipelines could serve as a "backbone" for broader transportation and communication routes linking the Caucasus and Central Asia to global markets.
2. Security reasons: Oil producers are reluctant to limit their exports to a single route because all proposed routes would pass through unstable territories in Chechnya, Georgia and Turkey-territories where dramatic political changes could happen over night. All countries involved will feel more secure if their own supply of oil is not dependent on a single country.
3. Regional cooperation: Building multiple pipelines also offers the best incentives for better regional cooperation and conflict resolution. Construction of pipelines crossing multiple boundaries presents some obstacles. However, by crossing boarders, the pipelines will make the countries of the region more interdependent, and therefore less likely to engage in armed conflicts.

Policy Issues

Resource Exploitation Rights in the Caspian

Uncertainty concerning which countries are legally entitled to exploit the resources of the Caspian Sea is a major obstacle to further exploration of Caspian shelf resources. In order to resolve these legal issues, all regions of the Caspian, including Iran, must reach an agreement. Iran claims that, until there is an agreement between all the littoral states,

agreements between Iran and the USSR made in 1921 and 1940 are still effective. Any attempt to divide the sea unilaterally will be unacceptable.

"Law of the Sea"

At issue is a disagreement as to whether the Law of the Sea convention applies to the Caspian. If it does, the maritime boundaries of the five states could be established based upon the "equidistant" division of the sea and undersea resources into national sectors. If the Law does not apply (because the Caspian is landlocked), the Caspian resources should be jointly developed. Russia and Iran favor a joint approach and argue that the "Law of the Sea" does not apply to the Caspian. However, because this approach would include Iran, it presents a major problem for American firms, which are forbidden to do business with Iran.

Russia - Kazakhstan Bilateral Agreement

Kazakhstan and Russia recently signed an agreement that assigned portions of the seabed to each state. However, Iran opposed the agreement because it does not want to lose its power to determine how Caspian resources are used. During Soviet rule, Iran and the USSR together explored the Caspian Sea and its resources. Accordingly, Iran had 50 percent say in any decisions regarding the Caspian. Now five states are laying claim to the sea. To preserve its ability to influence what takes place in all parts of the water body, Iran claims that a division of the seabed is not necessary. Iran contends that if just one of the five littoral states is against exploration of the shelf, exploration should be stopped.

Regional Conflicts

Development of the Caspian region's energy resources will require cooperation between countries and is likely to help foster greater stability and security in the region. The involvement and participation of Iran will directly affect the country's future economic prosperity, as well as political stability in the Persian Gulf region.

Environmental Issues

Increased production in the Caspian region will increase pollution in the already considerably polluted Black Sea and Bosphorus Straits. Although no major oil spills or other accidents have occurred, the impact of heavy tanker traffic is evident. As traffic has increased, accidents in the Bosphorus have become more common, putting both the local environment and the inhabitants of Istanbul at risk. Some 60 ships carrying oil and other hazardous products pass through the Straits each day.

Turkey's recently passed regulations on stricter use of the Bosphorus have resulted in costly delays for oil and gas shippers, and these delays are only expected to increase. The flow of oil from Novorosiisk has already more than doubled. If Kazakh oil is also exported via Novorosiisk, congestion in the Straits will only grow, along with the potential for environmental catastrophe. Pipeline options that bypass the Black Sea and Bosphorus Straits are much less environmentally dangerous.

U.S. Unilateral Sanctions against Iran

The main obstacle to the Iranian pipeline option is the U.S.-imposed economic sanctions against Iran. The sanctions will adversely affect all countries that hope to participate in Caspian oil and gas development. The United States is making every effort to discourage the governments of the new Central Asian Republics from entering into agreements with Iran, and more importantly, from exporting their oil and gas through Iran to the Persian Gulf.

The U.S. government's current policy towards Iran is based on the U.S position that:

- Iran supports international terrorism;
- Iran is developing its military capabilities and supports the development of weapons of mass destruction;
- Iran opposes the Arab-Israeli peace process; and
- Iran represents a destabilizing political force in the region.

The Iran-Libya Sanctions Act illustrates several problems with U.S policies:

- The accusations regarding Iran have been greatly exaggerated. There is little evidence to suggest that Iran harbors aggressive ambitions in the Gulf. Although Iran has procured sophisticated missiles, other Arab Gulf States have similar missile capabilities. In fact, Iran has been substantially reducing its military spending due to financial problems. Iran has offered financial support to extremist Islamic groups, but the United States' recent charges of direct Iranian responsibility for specific terrorist acts against Israeli are doubtful.
- Some aspects of U.S. policy contradict international legal norms as well as specific international agreements. There is no legal or moral basis for gaining UN support for the sanctions. Accordingly, the United States' attempts to gain support from other nations were not only unsuccessful but also could result in greater alienation of America's strongest allies.
- The policy of "dual containment" of Iran and Iraq is not working. The United States' allies won't support or accept broad-based sanctions, even though the international community agreed to impose sanctions against Iraq. The United States' efforts to isolate Iran have been counterproductive and will continue to be unless its policies are changed.
- The Iran sanctions also hinder the United States' ability to support and participate in the development of the newly independent states of the former Soviet Union. The United States claims it wants to help these states become truly independent and less reliant on Russia. It also has been outspoken on the importance and international significance of the Caspian resources. However, the United States still favors routing pipelines through Russia and refuses to consider the least expensive and safest route: the Iranian route.
- The United States' current position ignores the fact that Iran's revolution has not spread. The Gulf is now politically stable; oil continues to flow; and Iran's economy is suffering as foreign investment has slowed.

Implications and impacts of the Iran-Libya Sanctions

According to the scholars at the Institute for International Economics, the United States' sanctions have:

1. Delayed new investment in Iranian oil and gas fields;
2. Imposed costs on U.S. firms and workers that would normally compete for sales to and

investments in Iran;

3. Incited U.S.-European tensions and restricted cooperative efforts in support of U.S. policy objectives;

4. Induced no significant change in Iranian policy; and

5. Complicated American foreign policy.

First and foremost, the U.S. sanctions against Iran are harmful to the United States itself. Trade restrictions cause job and income losses and higher prices for energy resources. They also sour relations with allies. The political objective of sanctions does not justify these costs. The United States' current policy will greatly damage its other interests in the Caspian region. It should switch to a policy of constructive engagement.

The Importance of Iran

Using Iran as an export route for Caspian energy resources will greatly enhance the profitability of these resources and the contribution they can make to developing Central Asian economies. Thus, political pressures aimed at isolating Iran will reduce the benefit of these resources for Central Asian economies.

Iran is already making efforts to advance its interests in Central Asia by expanding its commercial ties there. It has already started negotiating deals with Turkmenistan and Kazakhstan and should be recognized as an important player in Caspian region development.

Possible Outcomes

· U.S. Competitiveness. The United States' recent decision to waive secondary sanctions against European companies that invest in Iran has left American companies sitting on the sidelines of energy resource development in Central Asia. The U.S. sanctions have the perverse effect of penalizing U.S. companies as their European counterparts enjoy business profits made in Iran. Because European firms already have claimed most of the Iranian market, U.S. firms, and therefore American workers, will likely feel the effects of the sanctions long into the future, even if they were to be immediately lifted. While the aggregate cost in relation to the United States' total GDP is miniscule, the cost for individual firms and industry is significant. Recent research by the Institute for International Economics (IIE) calculated the domestic cost of the United States unilateral sanctions. The research found that, in 1996, U.S. exports to the 26 countries subject to U.S. sanctions (including Iran) were \$15 to \$19 billion lower than they would have been in the absence of the sanctions. If these lost sales are not offset by exports to other markets, IIE found that employment among U.S. export industries would be reduced by 200,000 or more jobs, and that this shift in employment would result in an export sector loss of \$800 million to \$1 billion annually. The longer the sanctions remain in force, the greater the impact to the U.S. economy and workers.

· Impact on Iranian policies. The United States' sanctions have not produced their desired effect; they have not prompted changes in Iranian policies. The election of President Khatami, however, shows that within Iran there is some level of dissatisfaction with

domestic policies. And Khatami has shown signs that he is interested in opening up the Iranian economy, as well as engaging in a dialogue with the United States.

U.S. Domestic Political Issues

The substantive goals of the United States' policy towards Iran are to reduce terrorism, terminate the production of weapons of mass destruction, and obtain Iran's cooperation in the Middle East peace process.

American policymakers generally view Iran as a threat to the international community. They believe Iran is the biggest sponsor of international terrorism and are concerned about its potential development of nuclear weapons. Accordingly, Congress and the Administration are reluctant to rethink American policy and change the United States' relationship with Iran. Nonetheless, recent signals from Khatami, Iran's newly elected president, increase the plausibility of opening a dialogue.

Issues that will need to be addressed in developing a strategy to push the Administration toward opening a dialogue with Iran and allowing U.S. firms to invest in Iranian pipeline projects include:

- Congress' lack of support for an official dialogue with Iran.
- Americans' biased and narrow knowledge of Iran and its policies.
- Americans' inadequate understanding of Iran's importance in the Caspian region.
- The fact that the Pentagon and other national security managers still direct the United States' policies toward Iran
- The mutual distrust between Iran and the United States.

Comprehensive Strategy

The objective of the following strategy is to convince U.S. government officials to support Iranian pipeline routes. The first step should be to persuade the Administration to ease its economic sanctions against Iran. U.S. Oil will need to persuade U.S. government authorities to rethink the United States' relationship with Iran and implement policies that will improve U.S.-Iran relations.

The strategy includes both short-term and long-term objectives. The short-term objective is to obtain a limited waiver of the sanctions to allow U.S. companies to engage in construction of an Iranian pipeline and/or allow swapping arrangements with Iran. The long-term objective is to persuade the U.S. government to lift the economic sanctions entirely.

The following pages lay out a domestic strategy, which includes four sub-strategies (a coalition building strategy, legislative strategy, media strategy, and negotiation strategy for approaching the U.S. government). Subsequently, international coalition building and media strategies are provided, as well as a bilateral strategy for U.S. engagement with Iran.

Domestic Strategy

Coalition Building Strategy

The Coalition for Caspian Energy Development (CCED) will consist of major American oil and gas companies doing business in the Caspian Region, as well as selected trade and industry associations, and other interest groups. CCED's objective will be to persuade the Administration and Congress to support an Iranian pipeline and grant a limited waiver to allow American companies to participate in building this line.

Toward this end, CCED will work to build support for mitigating if not ending the United States' sanctions against Iran. Specifically, CCED will work to raise national and international awareness of the negative effects of these sanctions. CCED will use this heightened awareness to pressure the Administration to revise its policies toward Iran. U.S. government agencies that will be approached include the State Department, Department of Energy, Department of Transportation, Department of Commerce, and the U.S. Trade Representative's office.

CCED will also draft and promote legislation that waives the sanctions for American oil companies.

In the long run, the Coalition will not limit its membership only to the energy industry, but rather identify other industries, such as agriculture, that would like to see changes in the U.S.-Iran relationship.

U.S. Oil has sufficient resources to begin forming the Coalition. Since the majority of Coalition members will be oil and gas companies, producers and organizations, sufficient financing is expected. In the long run, however, broadening the Coalition to other sectors will help with financing and will help in making a convincing case for lifting the sanctions.

The Coalition will work closely with other broader based coalitions such as USA*Engage, which is already addressing unilateral sanctions issues including the implications of sanctions for trade and the U.S. economy. With the help and support of USA*Engage, CCED will attempt to identify other industries that face difficulties associated with the Iran sanctions.

Membership

The following firms, corporations and organization will be targeted as potential members and supporters of the coalition.

US Oil corporations/producers U.S Associations
Mobil Corporation (recent merger with Exxon) American Petroleum Institute
Chevron USA*Engage Coalition
Exxon Association of Oil Pipelines

BP- Amoco Petroleum Equipment Institution

Texaco

Shell Oil (USA)

Unocal

Sun/Oryx,

Pennzoil

Arco

Enron

Philips Petroleum

Other groups

The coalition will also explore the possibility of involving the U.S. Chamber of Commerce in its efforts. In the long run, the Coalition will target membership drives at other industry sectors that also face losses due to the United States' sanctions against Iran. Agricultural groups, for example would also like to be able to do business with Iran. The United States' recent decision to ease sanctions on the sale of agricultural goods to Iran will only encourage agricultural groups' interest in our efforts.

Core members

Nine companies will form the core membership of the coalition in the United States. Thus the membership fees of these companies will pay the dues and the budget of the coalition. The fee will be the same for every company and newcomers will be charged the same amount. The core members will appoint a person who will be responsible for lobbying members of Congress from their respective districts. Additionally, company presidents and CEOs will be expected to give testimony before the appropriate congressional committees.

Supporting members

American trade and industry associations and other interest groups will give congressional testimony and generate supporting research and analysis.

Staff

The Coalition will establish a steering committee that will be responsible for making all decisions for the Coalition. The Coalition will also hire one full-time person to act as an organizer and administrator for Coalition functions. The staff person will also write Coalition newsletters, oversee the creation of a web page, and act as a liaison between all core companies and supporting members.

Legislative Strategy

- Objectives:
Convince the Administration and Congress that improving U.S.-Iran relations should be a top priority.
- Convince the U.S. government to relax or modify current sanctions against Iran to allow U.S. coalition members to pursue Iranian pipeline development.
- Convince U.S. officials that Iran is an important and influential state in the Caspian region.

- Convince U.S. officials that the Iranian pipeline option is the best option for both commercial and environmental reasons.

The legislative strategy focuses on both state and national governments. The first step for the Coalition will be to form a working group to develop proposed policies and a lobby group that will meet with members of Congress and Administration officials.

Next, the working group, with input from the lobby group will begin preparing legislation that would waive the sanctions for oil companies. The groups will also prepare an information packet to present to all members of Congress and appropriate Administration officials.

The information packet will include:

1. A white paper and a "Dear Colleague " letter (see exhibit);
2. A map of all possible pipeline routes;
3. A table that includes all data, including pipeline capacity, taxes, tariffs and the estimated cost of each pipeline project; and
4. Case studies done by potential pipeline investors.

Another packet of documents will concentrate on the Iranian sanctions and will include the following:

1. The Institute for International Economics' study on unilateral sanctions;
2. A cost-benefit analysis of companies that are prohibited from doing business in Iran; and
3. A report on the benefits of improving the United States' relationship with Iran.

Lobbying the U.S. Congress

Each member of the coalition will be responsible for lobbying members of Congress from their districts and states.

This task will include the following activities:

-District Meetings. Coalition members will meet with congressional and state elected officials and staff members to explain the Coalition's goals.

-Lobbying activities. These will include writing letters and making phone calls to influential members of Congress. Other lobbying activities will include:

- Persuading supportive members of Congress to write "Dear Colleague" letters to other members of Congress.
- Convincing appropriate congressional committees and subcommittees to hold hearings on Caspian pipeline options.

In addition, each coalition member will be responsible for lobby the following influential committee members:

HOUSE

1. Bill Archer - Chairman, House Committee on Ways and Means
2. Philip Crane - Chairman, House Subcommittee on Trade
3. Benjamin Gilman - Chairman, House Committee on International Relations

4. Ileana Ros-Lehtinen - Subcommittee on International Economic Policy and Trade
5. Barbara Cubin (R-WY) - Subcommittee on Energy and Chemical Resources
6. Joe Barton - Chairman, Subcommittee on Energy and Power

SENATE

1. Jesse Helms (R-NC) - Chairman, Foreign Relations Committee
2. Joseph Biden (D-DE) - Subcommittee on Intentional Economic Policy, Export and Trade Promotion

Lobbying USTR and the Departments of Commerce, State and Energy

The support of governmental agencies such as the Department of State, the Department of Commerce, the Office of the U.S. Trade Representative, and the Department of Energy is critical. Accordingly, Coalition members will meet with all government officials that are responsible for the Caspian region. Information packets similar to those prepared for Congress will be distributed to these administration officials.

Specific goals for these lobbying activities include:

- Convincing the Clinton Administration and Congress to engage in a dialogue with Iran.
- Pressing the Administration and Congress to consider the harmful effects of ILSA.
- Gaining support for the implementation of sanctions reform legislation.
- Gaining support for a limited waiver for American business interests in Caspian region energy resource development.
- Persuading the Administration to invite an Iranian delegation to the United States or offer to meet a delegation in a neutral third state.
- Persuading the Administration to support the Iranian option as an alternative pipeline route.

The Coalition should target and gain support from the following possible allies:

- Donohue - Chairman of US Chamber of Commerce
- Henry Precht - US Foreign Service Office, Iranian desk
- Trent Lott (R-MA) - Senate Majority leader
- Lee Hamilton (D-ID) - House Representative
- Bob Ney (R-OH)
- Richard Lugar - Senator
- Richard Gephardt (D) - Minority leader, House of Representative

The coalition should concentrate on the task of lobbying Congressmen who are the strongest supporters of sanctions, including:

- Jesse Helms - Senator
- Dan Burton (R-IN)-House Representative
- Mitch McConnell and Joseph Biden - Senators, Members of Task Force on Economic Sanctions.

Department of Defense officials will also need to be lobbied.

Media Strategy

Our main objective in using the media is to show the American public and American policymakers that sanctions do more harm than good because of their negative impact on American businesses and jobs. Our secondary objective is to change Americans' perception of Iran and the Iranian people. Through the media, the Coalition can show that America's negative view of Iran is not only biased but also greatly exaggerated.

CCED will use all available media tools in order to create greater visibility of the pipeline issue. However, it is important for U.S. Oil, as well as for all members of the coalition, to plan its media strategy and proceed with it very carefully so that the public does not view the Coalition as supporting terrorism. The Coalition should include in its media releases the message that oil producers are concerned about terrorism and the development of weapons of massive destruction. The Coalition should emphasize that its primary goal and interest is to benefit American businesses and workers.

The Coalition should also use the media to:

Highlight how the U.S. unilateral sanctions on Iran impact the U.S. economy, U.S. employment and U.S. competitiveness.

§ Present data that show how American firms are losing important business opportunities to European and Asian firms that are investing in the Caspian region and Iran.

§ Present data that show American investment in the Caspian region and show how the lack of oil transportation routes limits the region's potential.

· Highlight recent positive changes in Iran including its democratic election of President Khatami.

· Highlight the strategic importance of the Caspian region and the role of Iran in that region.

Although the issue of Caspian resource development is not going to attract the attention of the general public, the Iranian and unilateral sanctions issues could attract substantial attention from the general public and interest and ethnic groups. The sanctions issue should be addressed on a national level.

As part of a comprehensive media strategy, the Coalition will:

· Hold a press conference to announce the establishment of the Coalition for Caspian Energy Development (to be held in Washington, DC).

· Give speeches on the issues.

· Participate in televised debates on Iranian and pipeline issues.

· Place op-ed pieces in major newspapers and magazines such as the Washington Post, New York Times, Wall Street Journal, Financial Times, and Economist.

National Press, TV and Radio

1. Initiate a national debate on the Iranian issue through letters, editorials and op-ed pieces in the national and local press.

2. Offer TV and radio interviews with experts on the unilateral sanctions issue, experts on the Caspian region, and experts on Iran.

3. Offer stories to the print press concerning the Caspian region and Iran, their cultures and people and recent positive political changes.

4. Initiate a debate between influential experts who are for and against sanctions.
5. Initiate TV shows where policymakers, professors, journalists, scientists, writers and other representative of non-profit organizations meet and discuss the United States' and Iran's mutual interests.
6. Work with the American Petroleum Institute and other trade associations, magazines, and newsletters to place articles concerning the negative impact of unilateral sanctions on the U.S. economy, U.S. competitiveness, U.S. oil producers and development of the Caspian region.
7. Publish a monthly newsletter to inform interests groups, associations and the press on its progress.

Unpaid activities

§ Work with local and national newspapers and television to inform the public about the Caspian region and Iran and the key issues surrounding both regions.

§ Initiate a public debate among CEOs and/or Vice-Presidents of oil companies, industry associations, interests groups and elected officials on the transportation issues in the Caspian region and the pros and cons of unilateral economic sanctions as an American foreign policy tool.

§ Write op-ed articles for major newspapers and magazines such as the New York Times and the Economist.

Paid activities

- Place advertisements in major newspapers, such as the New York Times, Financial Times or Washington Post.

Business to Government Negotiation Strategy

The negotiation strategy identifies the different interests of all parties and details options for how U.S. oil companies can push the U.S. government toward relaxing its sanctions against Iran. Although these "negotiations" will take place informally over time, the Coalition will need to be prepared by identifying who its allies and opponents are, and also what their interests, options, and preferred outcomes are (see exhibit). Identification of all these elements will help the Coalition determine the best approach to take with different government authorities.

Problem

Construction of the chosen Main Export Pipeline (Baku - Ceyhan) has been put on hold indefinitely. This route, although politically appealing, is not commercially sound. The best route is the Iranian pipeline. However, because of the U.S. sanctions against Iran, American companies can not participate in its development. European and Asian firms are already investing in swapping oil with Iran; U.S. companies are missing business opportunities.

U.S. Oil's Preferred Outcome

Given the recent positive developments in Iran, U.S. Oil wants to convince the U.S. government and Congress to pursue a policy of constructive engagement with Iran and begin taking small steps toward building trust between the two countries. The long-term preferred outcome is to see the sanctions lifted entirely. The short-term preferred outcome is to obtain a waiver to ILSA so that American companies can participate in the development of Caspian region energy resources.

Best alternatives to a full waiver for U.S. oil companies is to get the U.S. government to agree to:

1. Allow U.S. companies to negotiate deals and explore business opportunities with Iran, but make the implementation of these deals contingent on sanctions being lifted. This has been done in the past. U.S. companies were allowed to negotiate commercial projects under the same conditions until the embargo on Vietnam was lifted in 1994.
2. Allow U.S. companies to engage in swapping arrangements with Iran. Currently, U.S. Oil ships its share of Turkmen crude across the Caspian Sea and then by rail to the Black Sea. This route is costly, is subject to delays, and carries significant environmental risks.
3. Grant U.S. companies a limited waiver to use Iranian equipment in the Caspian. This policy will help U.S. companies in two ways. First, U.S. companies would not be excluded from important energy development in the Caspian just because some partner companies use Iranian supplied equipment. Second, Iran owns the most conveniently located emergency equipment. Therefore, if a spill or other environmental problem were to occur, U.S. companies would be able to pull together all available resources and equipment to deal with the problem

Allies

- American investors in the Caspian region
- The U.S. Chamber of Commerce
- Other companies and industry sectors, such as agriculture, that are interested in seeking business opportunities in Iran
- Established coalitions, such as USA* Engage, that are concerned by the United States' use of unilateral sanctions
- Companies that are already members of USA*Engage
- The National Foreign Trade Council
- Foreign governments, including Kazakhstan, Azerbaijan, Turkmenistan and Russia, that favor the Iranian pipeline option. (Since United States firms account for the largest amount of investment in the Central Asia, however, these governments do not want to provoke the U.S. government and therefore will only give limited support to the Coalition's efforts.)

Talking Points

U.S. Oil should stress that it is concerned with terrorism and weapons development issues, but that the sanctions are ineffective and are harming U.S. companies, U.S. workers, U.S. competitiveness, and the U.S. economy. U.S. Oil should also point out that the recent waiver of secondary sanctions weakened America's position relative to its European and Asian competitors in the Caspian region. Additionally, the following points should be made:

- Iran is an important player in the Gulf and the Caspian region.
- Continuing to isolate Iran will have a negative impact on Caspian region development.
- A pipeline that takes oil to Asian markets is needed.
- The advantages of the Iranian route outweigh its disadvantages. The route is commercially viable, and it presents less environmental risk than other routes. Moreover, whereas other routes pass through politically unstable areas, Iran is a stable and unified nation.
- U.S. Oil should be allowed to take commercial steps that would be regarded as positive American gestures towards Iran. U.S. Oil should be allowed to participate in the construction of an Iranian pipeline and swapping arrangements, and it should be allowed to use Iranian equipment. Finally, U.S. Oil should be allowed to negotiate business deals with Iran-deals that would be implemented only if sanctions are lifted.

Objective Criteria

- An official feasibility study of the commercial viability of the Iranian option.
- A list of European and Asian companies that are investing in the project in Iran.
- Statistical data on the potential profits from those investments.
- Information about the recent decision to allow American agribusiness to sell its products to Iran.

Best Alternative to a Negotiated Agreement (BATNA)

- Invest in other pipeline routes.
- Pursue legal action against the U.S. government.
- Seek a re-imposition of broad international sanctions to limit the foreign competition's ability to profit from an Iranian pipeline.
- Withdraw all investments in the Caspian region.

INTERNATIONAL STRATEGY

Objectives:

This strategy is designed to generate broad support from international governments, organizations, and businesses in order to convince the U.S. government to change its current policy toward Iran. The international community can bring attention to the issue and help accelerate efforts to resolve it.

The following actions need to be taken:

Ø Establish an International Coalition for Caspian Region Economic Development (ICCRED).

The Coalition for Caspian Energy Development (CCED) will take a leading role in establishing and guiding ICCRED. The governments of the Caspian region states, including Georgia and Turkey, should be invited to become members of the group. Other potential members are international oil companies such as BP, Agip, Total, Dutch Shell, LukOil, Petronas, British Gas, and Elf. In addition, ICCRED should invite participation from U.S. Chamber of Commerce representatives located in the Caspian region.

ICCRED should take the following actions:

1. Work to influence the U.S. government to allow the construction of an Iranian pipeline.
2. Press the United States to reform its legislation on sanctions.
3. Convince the U.S. that the Iranian pipeline is the best option, at least until the MEP is built.

Ø Initiate an International Media Campaign.

The primary objective of this strategy is to generate public awareness of the need to change the United States' long-time negative relationship with Iran. The campaign will be primarily focused on educating the general public about the Iran-U.S. relationship, the evolution of this relationship, and recent positive developments in Iran. In addition, the campaign will emphasize the negative and harmful impact the unilateral sanctions have on the United States' economy and U.S. jobs.

The following actions should be taken:

1. Hold a press conference to announce the establishment of ICCRED.
 2. Pitch news features to and place op-ed pieces in major newspapers in London, Paris, Moscow, Kazakhstan, Turkey, Georgia, Italy and other countries.
-

U.S.-Iran Bilateral Strategy

Problem

USA*Engage and other groups have provided testimony detailing the negative impacts of the U.S. sanctions against Iran. The U.S. government is fully aware of the negative consequences of the sanctions and that the Iranian issue greatly affects development prospects in the energy rich Caspian region.

In light of the positive signals from president Khatami, the time is ripe for the United States to consider opening a dialogue with Iran. If the United States continues to isolate Iran, it will likely harm a wide range of other U.S. interests.

Preferred Outcome of the U.S. Government

1. Continue to isolate Iran (and oppose any pipeline routes that involve the country) as a means of denouncing Iran's support for terrorism, support for the development of weapons of mass destruction, and attitude towards the Middle East Peace Process.

Interests

1. Continue to oppose Iranian policies, its support of terrorism and production of weapons of massive destruction.
2. Support Turkey (a U.S. ally) by supporting development of the Baku-Ceyhan MEP.
3. Encourage the private sector and financial organizations to bear the cost of building the pipeline to Ceyhan.

Options

1. Allow U.S. firms' participation in the construction of an Iranian pipeline as a means of establishing a foothold in Iranian oil and gas exploration and development.
2. Engage in a "constructive dialogue" with Iran, with the goal of entering into an official dialogue.
3. Take intermediate steps that will pave the way towards more open U.S.-Iranian relations. The United States could:
 - Allow an American fact finding mission to go to Iran and conduct an analysis of the political climate, economic position and overall situation in the country.
 - Invite an Iranian delegation to the United States.

Recommendations

Washington should:

1. Broaden its view of Iran and respond to positive developments in the country.
2. Begin taking small steps that could lead to an official dialogue.
3. Send positive messages to the Iranian people using all possible means, including interviews, and Iranian radio and TV.
4. Change the U.S. visa policy for Iranian people.
5. Bring experts on Iran and the Caspian region together and initiate a TV debate or show.
6. Establish an exchange program for students and scholars.
7. Address historical events, including the 1963 coup, the U.S. role in the 1979 revolution and the 1979-81 hostage crisis (however it is critical to focus on the future and the potential for a constructive dialogue).
8. Grant licenses to U.S. companies to engage in business activities with Iran.
9. Invite Iran to joint the Middle East North Africa (MENA) economic conference.

NOTE: The above actions should not be unilateral but reciprocal. The United States should expect the Iranian government to take complementary steps and demonstrate a willingness to change.

Best Alternative to a Negotiated Solution (BATNA)

1. Do nothing and continue the sanctions.
2. Wait to do anything until oil prices are higher and the financial crisis in the Caspian region is over.

APPENDIX A

Export Pipeline Routes

Firms Projects	Pipelines	Capacity,bb/y	Tariffs \$/barrels	Cost \$ millions
----------------	-----------	---------------	-----------------------	------------------

CPC (Caspian Pipeline Consortium)	Tengiz-Black Sea (Novorossisk)	67	25	2197 (today this project estimated at 4500)
AIOC	Baku-Tbilisi-Suspa (917km)	25	14,21	1000-1500
Brand&Rood (USA)	Tengiz-Aktau-Mahachkala-Tbilisi-Ceyhan (Turkey)	45	41.2	3620
Amoco	Kazakhstan-Baku-Supsa (1620km)		25,1	2260-2700
Amoco	TransCaspian pipeline Baku-Ceyhan (1710)	50	26,18	2300-3500
Amoco	Kazakhstan-Baku-Tbilisi-Ceyhan (2430km)	45	36,4	3500-4200
BOTAS (Turkey)	Kazakhstan-Turkmenistan-Azerbaijan-Georgia-Turkey		43,5	2188
Total (France)	Kazakhstan (Tengiz)-Turkmenistan-Iran (2511km)	1 Variant-25 2 Varian-50	26 20,1	2700 4000

APPENDIX B

Caspian Sea Region Oil Production and Exports
(thousand barrels/day)

	Production (1990)	Production (1996)	Exports (1990)	Export (1996)
Azerbaijan	259.3	198.7	76.8	42.6
Kazakhstan	602.1	532.1	109.2	254.5
Turkmenistan	124.8	103.9	69.0	26.4
Uzbekistan	86.2	182.6	-168.1	3.8
Russia* *	62.0	52.0	0.0	0.0

* Only the regions near the Caspian are included

* * Includes these regions bordering the Caspian Sea: Astrakhan, Kalmyk Republic

APPENDIX C

Oil and Gas Reserves in the Caspian Region

	Proven Oil Reserves	Possible Oil Reserves	Total Oil Reserves	Proven Gas Reserves	Possible Gas Reserves	Total Gas Reserves
Azerbaijan	3.6-11.0BBL	27 BBL	31-38BBL	11 Tcf	35 Tcf	46 Tcf
Kazakhstan	10.0-16.0BBL	85 BBL	95-101BBL	53-83Tcf	88 Tcf	141-171Tcf
Russia*	0.2 BBL	5 BBL	5 BBL	N/A	N/A	N/A
Turkmenistan	1.4-1.5 BBL	32 BBL	34 BBL	98-155Tcf	159 Tcf	257-314Tcf
Uzbekistan	0.2-0.3 BBL	1 BBL	1 BBL	74-88 Tcf	35 Tcf	109-123Tc

* Only the regions near the Caspian are included
 BBL = billion barrels, Tcf = trillion cubic feet

APPENDIX D

Oil Export Routes in the Caspian Sea Region

	Route	Crude Capacity	Length	Investment	Status
AIOC-Main Export Pipeline	Multiple routes considered from Baku (Azerbaijan)	1 million barrels/day	1100 miles if to Ceyhan, Turkey	\$3.3 billion if to Ceyhan, Turkey	Final Route Selection
AIOC-Early Oil Western Route	Baku (Azerbaijan)-Supsa (Georgia)	0.1 million barrels/day	550 miles;	\$290 million	Exports begin late 1998
AIOC-Early Oil Northern Route	Baku (Azerbaijan)-Novorossiysk (Russia) via Chechnya	0.1 million barrels/day	868 miles; 90 miles are in Chechnya	\$2.4 billion repairs to Chechen line	Exports begin late 1997-early 1998
Northern Route Early Oil-Chechnya bypass	Azerbaijan/Russia border-Terskoye (Russia) via Dagestan	N/A	176 miles	\$220 million	Announced 9/97; tender planned
Caspian Pipeline Consortium	Tengiz (Kazakhstan)-Novorossiysk (Russia)	1.34 million barrels/day peak	930 miles	\$2.2 billion	Flows 1999; peak early next decade
Cross-Caspian	Tengiz-Baku or Turkmenbashi-Baku	0.4-0.5 million barrels/day	Underwater 370 miles or 190 miles	\$2.5-\$3.0 billion	Feasibility study

Kazakhstan-China (may extend to Turkmenistan&Uzbekistan)	Aktubinsk (Kazakhstan)-Xinjiang (China)	0.4 million barrels/day rising to 0.8 million barrels/day	1,800 miles	\$3.5 billion	Signed Agreement
Turkmenistan-Afghanistan-Pakistan (may extend to Uzbekistan)	Charjou (Turkmenistan)-Gwadar(Pakistan)	1 million barrels/day	1,000 miles	\$2.5 billion	Memorandum Understanding for this Central Asia Oil Pipeline Segment
Turkmenistan-Persian Gulf (may extend to Kazakhstan)	Turkmenbashi (Turkmenistan)-Kharg Island (Iran)	0.2-0.4 million barrels/day	930 miles	\$1.5 billion	Proposed

APPENDIX E

WHITE PAPER

One of the most logical, inexpensive and commercially viable export routes for Caspian region energy resources is a pipeline through Iran. However, the United States does not support building an Iranian pipeline. In fact, the United States' policies and unilateral economic sanctions against Iran are the biggest constraints in the development of the Caspian's vast energy resources.

While the region is one of the most commercially important areas of the Newly Independent States because of its oil and natural gas reserves, American companies have not been able to fully participate in the development of this region because of the United States' sanctions against Iran.

Most governments, including the U.S. government, support building an East-West, Baku-Ceyhan pipeline. This route, however, is not commercially viable. It is one of the longest and most expensive routes, and with today's low oil prices, revenues would not justify expenses. Until Caspian region oil exports grow significantly, this project (although it has already been approved) will not move forward. The private sector will not risk investment in Caspian oil and gas development unless there are commercially viable transportation routes for getting these resources to world markets.

Among the other pipeline options, the Iranian pipeline option makes the most sense. The Iranian route would be the cheapest and fastest to build, and because it avoids the Black Sea and the Bosphorous Straits, it presents far less environmental risk.

The United States' sanctions prohibit American producers from engaging in any business activity with Iran. The sanctions were imposed because the United States views Iran as a sponsor of international terrorism and fears that Iran is trying to acquire nuclear weapons. In fact, however, U.S. companies have been hurt most by the sanctions because they have been denied the opportunity to invest in Iran and engage in other profitable arrangements, including swapping arrangements and contracts to use Iranian equipment. The U.S. sanctions have only given foreign firms the opportunity to profit where U.S. firms cannot. European companies in particular are investing in multibillion-dollar projects offered by the Iranian government and thereby undermining U.S. companies' competitiveness, as well as the effectiveness of the sanctions.

Indeed, European firms have already claimed most of the Iranian market. Recently the French oil company Total announced a \$2 billion contract to develop Iran's offshore gas fields. The Asian firm Petrona has also signed a multimillion dollar project. And a consortium of French, Italian and Iranian oil companies have signed a \$998 million, 10-year contract to redevelop a giant oil field in Iran. Elf Petroleum Iran, a subsidiary of the French Oil Company Elf Aquitaine will be the lead partner.

Because Iran is a major player in the Caspian region, U.S. policy on Iran contradicts its interests. Iran has close cultural and religious links to the Caspian states, and it will play an important and unique role in the development of Caspian resources. U.S. policy won't change this reality. And it will be impossible for the United States to participate in Caspian region development in any meaningful way unless it changes its relationship with Iran.

APPENDIX F

Congressional Testimony

Statement of Bill Slick, Chairman of U.S. Oil Company
& President of the Coalition for Caspian Energy Development

Testimony before the House Subcommittee on
International Relations and Trade

Good afternoon. Thank you Mr. Chairman and members of the Subcommittee for giving me this opportunity to speak before you today. I am Bill Slick, Chairman of U.S. Oil Company and President of the Coalition for Caspian Energy Development or CCED. I am here today on behalf of U.S. Oil Company and CCED to address our concerns over

U.S. policy towards Iran and to ask for support of legislation that will reform current sanctions against Iran.

Currently, U.S. companies are prohibited from engaging in any business activities with Iran due to the United States' unilateral economic sanctions against this country. While the U.S. Administration supports free trade, it has banned all U.S. trade with Iran, an action which has cut U.S. oil companies out of several deals in the Caspian Sea oil fields and continues to prohibit them from participating in profitable projects. While Iran is opening up to foreign investments, American companies are left sitting on the sidelines.

More importantly, the Iranian sanctions have compromised U.S. companies' ability to compete in the strategically important and resource-rich Caspian region. Because Iran is an important player in Caspian resource development and controls a large amount of the oil extraction and refinery equipment in the region, foreign companies that are not restricted from doing business with that country have numerous options available to them whereas U.S. companies are severely limited.

We cannot ignore Iran. If the United States wants to participate in developing Caspian region economies, it must recognize that Iran is an important player in the region. The isolation of Iran cannot and should not continue. The United States would benefit greatly from building a more open and constructive relationship with Iran.

U.S. Oil is very interested in engaging in Caspian region pipeline development. The best pipeline option, however, is the Iranian pipeline option. Advantages of the Iranian pipeline include:

- It is commercially viable.
- It requires less investment in comparison to other pipeline options.
- It can be constructed faster than other pipeline options.
- It offers the best solution for near-term oil export.
- It avoids unstable political regions.
- It avoids the Black Sea and Bosphorus Straits where the risk of a disastrous oil spill is greatest.

-

The democratic election of President Khatami should be considered a positive development in Iran. The United States should respond by supporting the Iranian pipeline and granting American companies permission to invest in the Iranian oil and gas sector. Such a step would serve to open up the possibility of renewed U.S.-Iran relations. In fact, companies like U.S. Oil can act as a vehicle for changing the hostile relations between the two countries.

While U.S. Oil agrees with the United States' policy goals, unilateral sanctions are not the right tool for advancing these goals. Sanctions don't work; they don't change the behavior of a country, its policies or leaders. They do, however, punish ordinary citizens and prohibit companies from being part of great investment opportunities. Only the

United States continues to refuse to do business with Iran. So the sanctions are only creating barriers for U.S. companies.

The United States' policy toward Iran contradicts other U.S. policy goals. While the United State government wants to help the Central Asian republics grow and prosper, especially in the development of the area's large oil and gas resources, U.S. sanctions against Iran are creating roadblocks to U.S. companies involvement of such development.

As we near the end of the 20th century, barriers to trade and investment are falling, and countries, which have long been closed to foreign trade and investment, are now opening again. This is a great opportunity for the United States to rethink its current policy and open the door to Iran.

We urge the Subcommittee to pass a resolution in support of the Coalition for Caspian Energy Development's campaign to lift the U.S. economic sanctions against Iran.

On behalf of the Coalition for Caspian Energy Development, I thank you for your attention.

After my colleagues have testified, we welcome questions from the Subcommittee.

Thank you.

APPENDIX G

Letter to Coalition Member

Dear potential coalition member (a major U.S. oil company):

As the president of a corporation that is already involved in efforts to develop Caspian region energy resources, you are fully aware that there is still no good route for transporting these resources to world markets. I'm sure you agree that one of the most commercially viable and logical routes is the Iranian route. However, due to the U.S. economic sanctions against Iran, U.S. companies are prohibited from participating in developing and using this route. While countries of the Caspian region and our European allies are fully supportive of this route, and in fact are already setting up deals with Iran to move the project forward, U.S. oil producers are forced to sit and watch from the sidelines.

U.S. Oil is aware of the reasons behind the United States' policies toward Iran. However, we think that economic sanctions are the wrong tool for addressing issues of terrorism and the development of weapons of mass destruction. The United States' sanctions are not achieving these goals and, at the same time, the sanctions are causing U.S. companies to lose business, which means American workers are losing jobs too. Constructive engagement that allows bilateral trade and shared business investments would be a much more effective way to influence the Iranian government. Trade generates economic benefits to both countries.

U.S. Oil is forming both a Coalition for Caspian Energy Development in the United States and an International Coalition for Caspian Region Economic Development that will be established in Kazakhstan. The primary objective of CCED is to put pressure on the U.S. Government to consider allowing U.S. business participation in building the pipeline through Iran. CCED's long-term objective is to convince the U.S. government to pass legislation that recognize the need to lift the unilateral sanctions.

U.S. Oil would like your company to join the coalition and, by doing so, support our objectives and actions towards achieving those objectives.

I look forward to your response and will contact you in a few days to answer any questions you may have.

Sincerely,

Bill Slick
Chairman, Chief Executive Officer