

**Testimony by  
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**The Strategic Challenge Posed by Iran**

The behavior and the policies pursued by Iran's current leadership pose profound and wide-ranging challenges for our interests, for our friends and allies in the Middle East and in South Asia, and for the international community as a whole.

These policies include Iran's nuclear ambitions; its support for terrorist groups, particularly Hizballah, Hamas, and Palestine Islamic Jihad; its longstanding rejection of a two-state solution to the Palestinian-Israeli conflict; its efforts to sow violence and undermine stability in Iraq and Afghanistan, including lethal support for groups that are directly responsible for hundreds of U.S. casualties; and finally, the strategic implications of Iranian behavior for Gulf security. Across the broader Middle East, Iran's actions jeopardize the peaceful and prosperous future that the region's responsible leaders, with the support of the United States and the international community, are striving to build.

**Iran's Vulnerabilities**

Iran's vulnerabilities, and the complexities of Iranian society, need to be considered along with the challenges posed by Iran's behavior. For its part, Tehran seems to relish heightening concerns by promoting the illusion that Iran is on the ascendance. We are all familiar with the repugnant rhetoric, employed by some Iranian leaders intended to aggrandize Iran as a powerful counterweight to the U.S. as well as the institutions of global order, especially the United Nations and the International Atomic Energy Agency (IAEA). However, Iran is not ten feet tall, nor is it even the dominant regional actor. Iran's regime has some real insecurities - not least the widespread alarm and resentment that its policies and rhetoric have generated throughout the region and the international community at large. In the late 1990s, Iran endeavored to rebuild its ties to its neighbors and the world as a whole. However, today, Iran has no real friends anywhere that could offer strategic reassurance, vital investment, or a secure future in a globalized world. Many of its neighbors retain wary relations, its alliances are limited to a handful of countries, such as Syria, Belarus, Cuba, and Venezuela, and its destabilizing actions have drawn the international community closer in unprecedented fashion.

And, while Iran may benefit from a degree of instability in Iraq, Afghanistan, Lebanon, and the Palestinian territories, it is also facing a new and more challenging situation in many of these arenas. The complexities of internal politics and a revival in responsible regional diplomacy are complicating Iran's pursuit of regional hegemony.

In Iraq, for example, Iran's destabilizing activities are beginning to encounter new obstacles in the form of a more capable and coherent Iraqi government. Most Iraqi leaders want normal relations with Iran, but as the central government's capacity and confidence grows, its priority is to assert Iraq's own sovereignty. The Iraqi Security Forces' move into Basra earlier this year, and similar operations elsewhere in southern Iraq, in Baghdad, and now in northern Iraq are clear examples of indigenous Iraqi efforts to assert the central government's authority and counter Iraqi militants, including militias receiving Iranian support. Prime Minister al-Maliki's recent meetings in Tehran, where he lodged protests against Iran's support for terrorist groups in Iraq, made clear the limits to Iranian-enabled lethal attacks in Iraq. In addition, the readiness of the Iraqi government and security forces to confront Iranian-backed groups has also produced new support and cooperation from its Arab neighbors. So far, Bahrain, Jordan, and the UAE plan to send Ambassadors to Baghdad, and we hope other Arab governments will heed their example and do the same.

The Doha Agreement, which allowed a partial resolution of that crisis, is an example of a new and positive activism on the part of Arab governments, in part due to their concern over Iran's destabilizing activities and growing regional aspirations. The strong Arab role in the process sent a direct message to Iran that the leadership in Tehran will not be given free rein to further undermine the democratic process in Lebanon through its support to Hizballah. We are watching with interest Iran's relationship with Syria. Syria has begun indirect peace talks with Israel, and this follows Syria's attendance at last fall's Annapolis Peace Conference, a move that apparently surprised the Iranian leadership and led to some adverse commentary from Iran. Syria appears to be conducting a policy toward Israel that is independent from Iran's, presumably leading some in Iran to worry that in the future the extremely close relationship between the two governments could weaken.

We also see the concern of other governments translated into new cooperation and an expanding coalition of countries that oppose Iran's aggressive behind-the-scenes policies. Many regional governments that feel threatened by Iran are working more energetically to counter and diminish its influence in the region. This is evidenced by the changed dynamic between Iraq and its neighbors, including the reintegration of Iraq into regional affairs through its participation in Gulf Cooperation Council meetings with Egypt and Jordan in a GCC plus 3 configuration. In addition, Gulf nations participating in the Gulf Security Dialogue are working cooperatively among themselves and with the United States on security issues of mutual concern. These states support the responsible and transparent development of civilian nuclear energy but have publicly declared their opposition to the pursuit of nuclear weapons. To that end, in direct contrast to Iran, some regional governments have chosen to conclude nuclear cooperation agreements in partnership with the U.S., without the development of an indigenous fuel cycle, contradicting Iran's claims that the West seeks to prevent the pursuit of nuclear energy for peaceful purposes. This is also consistent with the choice made by South Korea, and others.

In addition to the political and diplomatic vulnerabilities Iran's leadership has created for itself, Iran's current leaders also confront well-documented internal challenges, the direct product of the current leadership's extraordinary economic mismanagement.

Ten years ago, we saw hopeful signs that Iran's government was slowly beginning to appreciate the political and economic imperatives of democracy. Today, unfortunately, those small steps toward moderation and greater popular participation have been all but erased by the hard-liners who hold sway in Tehran. The international community rightly criticized the Iranian government's treatment of its own people, and the regime's record of human rights abuse has only grown worse over this past year. The regime regularly commits torture and other forms of inhumane treatment on its own people – including labor leaders, women's rights activists, religious and ethnic minorities, and critics of the regime, severely restricts basic freedoms of expression, press, religion, and assembly to discourage political opposition, and manipulates Iran's electoral process, particularly through the mass disqualification of candidates.

It is an irony that despite its abundance of hydrocarbon resources, Iran's policies have made it necessary to rely on imports of refined petroleum products to meet internal demand. The Iranian government is failing its own people. Iran's nuclear activities may eventually cost billions of dollars, which could be better spent to benefit the Iranian people. Inflation in some sectors is running well above 25 percent—a heavy burden for the Iranian people and a profound vulnerability for the regime. Food and housing costs, especially in Iran's major cities, are high and rising. Many foreign investors, particularly from Iran's historic trading partners, are reluctant to commit capital in such a precarious political environment and while Iran continues to pursue threatening policies. Record oil revenues may sustain the regime for the time being, but thanks in large part to the disastrous policies pursued in recent years, this oil windfall has failed to generate the jobs, growth and diversification that Iranians desperately need. Iranians need only look across the Gulf – to the spectacular rise of an advanced, innovative economy in Dubai, the rapid expansion of Qatar's natural gas exports and gas-based industries, and the wise efforts by Saudi Arabia and other oil-rich states to reduce debt, undertake needed reforms, and invest in future capacity – to appreciate the opportunities squandered by their own leaders.

Iran's people aspire to more. Their population, two-thirds of which are under 30, have a mounting appetite for modernity, advanced technology, and the better relations with the international community that would derive from expanded trade and economic development.

We hope that the new dilemmas Iran is beginning to face at home, in the region, and in the broader international community, will provoke a serious reconsideration of its provocative policies, revive internal debates about the utility of moderation and responsibility, and move Iran toward a more cooperative and constructive path. Until that time, however, the U.S. and the international community remain committed to meeting the challenges posed by Iran.

### **The U.S. Response**

The purpose of our policy is to change Iran's problematic policies and behavior by making common cause with as much of the international community as we can. Our goal is to convince Iran to abandon any nuclear weapons ambitions, cease its support for terrorist and militant groups, and become a constructive partner in the region. As President Bush has said, "all options are on the table, but the first option for the United States is to solve this problem diplomatically." This requires tough minded diplomacy, maximizing pressure on the Iranians at multiple points to drive home the costs of continued defiance of the rest of the world, especially

on the nuclear issue. At the same time, however, we are trying to make clear to Iran and its people what they stand to gain if they change course. As Secretary Rice said at Davos earlier this year, “America has no permanent enemies, we harbor no permanent hatreds. Diplomacy, if properly practiced, is not just talking for the sake of talking. It requires incentives and disincentives to make the choice clear to those with whom you are dealing that you will change your behavior if they are willing to change theirs. Diplomacy can make possible a world in which enemies can become, if not friends, then no longer adversaries.”

This Committee is intimately familiar with the dual-track strategy that we have employed in concert with our P5+1 partners – the UK, France, Germany, Russia, and China – to put before the Iranian leadership a clear choice, so that it chooses a better way forward. Javier Solana’s June 14 visit to Tehran to present the updated incentives package was an essential element of this approach, stressing the significant political, economic, technological, and energy benefits that could accrue to Iran if its leaders chose cooperation over their current course.

President Bush emphasized last month at the US-EU Summit that we seek to address this issue through a multilateral framework. He said: “Unilateral sanctions don’t work...One country can’t solve all problems...A group of countries can send a clear message to the Iranians, and that is: ‘We are going to continue to isolate you. We’ll continue to work on sanctions. We’ll find new sanctions if need be if you continue to deny the just demands of a free world.’”

Consistent with the President’s vision, Iran’s failure to restore the international community’s confidence in its intentions has not gone without consequences. The UN Security Council has adopted four resolutions on Iran, including three imposing Chapter VII sanctions. While some have questioned the impact of these measures, we do see a tangible effect. Two and half weeks ago, the European Union adopted sanctions on 38 additional Iranian individuals and entities, including prohibiting business with, and imposing an asset freeze on, Iran’s largest bank, Bank Melli. The EU began formal consideration of additional measures last week. These actions, taken together, undermine Iran’s ability to portray this problem as a bilateral one, and also weaken Iran’s argument that the U.S. and the West are isolated in this cause.

The international community is more unified than in the past on the necessity for Iran to fully and verifiably suspend its proliferation sensitive nuclear activities and reestablish international confidence in the peaceful nature of its nuclear program. There is also a mounting consensus for Iran to come clean on its past efforts to build a nuclear warhead, based on the information presented in recent reports by the IAEA Director General which describe Iran’s continued failure to cooperate with the IAEA investigation into Iran’s weaponization activities.

While Iran seeks to create the perception of advancement in its nuclear program, real progress has been more modest. It is apparent that Iran has not yet perfected enrichment, and as a direct result of UN sanctions, Iran’s ability to procure technology or items of significance to its missile programs, even dual use items, is being impaired. In addition to limiting Iran’s access to proliferation sensitive technologies and goods, key individuals involved in Iran’s procurement activities have been cut off from the international financial system and restricted from travel, and Iran’s banks are being pushed out of their normal spheres of operation. Last November, Iran’s OECD sovereign credit risk rating was downgraded from a 5 to a 6, on a scale of 0 to 7, and as a

result, the cost of official export credit from OECD countries to Iran and its state-controlled enterprises has increased by approximately 30%, while availability of credit has shrunk. A number of export credit agencies have withdrawn or dramatically reduced exposure (notably those of the UK, Canada, Italy, and France), and almost all first tier banks have also withdrawn business from Iran.

The UN Security Council, U.S., and EU designation of Iranian banks further hinders Iran's reach. The most recent UN Security Council Resolution requires that states exercise vigilance with respect to the activities of banks in their jurisdictions with *all* banks domiciled in Iran and their branches and subsidiaries abroad. It mentions Banks Melli and Saderat, in particular. The Financial Action Task Force, a group composed of 32 countries including each of the five permanent members of the UN Security Council, has issued two serious warnings in less than a year, warning of the risks posed to the international financial system by deficiencies in Iran's anti-money laundering and counterterrorist financing regime. And the world's leading financial institutions have largely stopped dealing with Iran, and especially Iranian banks, in any currency. They do not want to risk unwittingly facilitating the regime's proliferation or terrorism activities. All of this adds up, keeping Iran on the defensive, forcing it to find new finance and trade partners and replace funding channels it has lost – often through more costly and circuitous mechanisms.

Government and private sector action on Iran has a psychological impact, as well. Iran has expressed its desire to assume the economic and political role it believes it deserves in the region, and to be seen as a legitimate player on the global stage. But the series of UN Security Council resolutions has shown the world – and Iran – that the international community will not allow an irresponsible actor such as Iran to expand its power unchecked. The effects of Iran's growing international stigma may, in the end, be as substantial as the direct economic impact of any sanctions. Losing the ability for a single Iranian bank, such as UN-designated Bank Sepah, to conduct business overseas is painful to Iran. Having major international financial institutions refuse to do any business with Iran because of the legitimate business risks that such trade present may be worse. This increasing pressure is only being amplified by the regime's own economic mismanagement, as it fails to deliver on its promises to improve the lot of average Iranians.

We have been working with our regional partners to help them develop the kind of cooperation that will help them better manage the political, diplomatic, and security challenges Iran poses. These efforts are beginning to show signs of success. Examples include inter-Arab cooperation to help dampen the political crisis in Lebanon, the Gulf Security Dialogue, and the new interest on the part of the Arab governments in dealing with the Government of Iraq.

Finally, in tandem with the diplomatic and financial measures that are focused on the Iranian regime, we remain committed to charting a new course for U.S.-Iranian relations by intensifying our engagement with the Iranian people, with the hope of bridging the divide. We are now in the second year of a successful people-to-people exchange program. Partnering with the U.S. Olympic Committee, we invited 15 members of the Iranian table tennis national team to the States last week. This group included the first female Iranian athletes who have ever been to the U.S. on this program. In cooperation with the NBA, we will bring 25 members of the Iranian

Olympic Basketball Team here next week for the NBA Summer League. We also hope to bring the Iranian soccer team to the U.S. later this year. Over the long-term, we hope to build connections among our people through educational, cultural, and other exchanges which can overcome 30 years of estrangement that has severed links between our societies.

The United States stands with the Iranian people in their struggle to advance democracy, freedom, and the basic civil rights of all citizens. We believe the Iranian people have made clear their desire to live in a modern, tolerant society that is at peace with its neighbors and is a responsible member of the international community. We are confident that if given the opportunity to choose their leaders freely and fairly, the Iranian people would elect a government that invests in development at home rather than supporting terrorism and unconventional warfare abroad; a government that would nurture a political system that respects all faiths, empowers all citizens, more effectively delivers the public services its people are asking for, and places Iran in its rightful place in the community of nations; a government that would choose dialogue and responsible international behavior rather than seeking technologies that would give it the capability to produce nuclear weapons and foment regional instability through support for terrorist and militant groups.

### **Looking to the Future**

In summary - -

We have presented the Iranian government with a historic opportunity to do two things: to restore the confidence of the international community in its nuclear intentions, and to give its own people the access to technology, nuclear energy, education, and foreign investment that would truly open the way to economic prosperity.

We have made clear that we do not object to Iran playing an important role in the region, commensurate with its legitimate interests and capabilities, but also that Iran is far more likely to achieve its desired level of influence if it works with the international community and its neighbors, rather than if it works against them. We recognize that it would be useful for Iran to be “at the table” on major international matters if Tehran is willing to contribute in a constructive fashion.

The dual-track strategy to which we often refer in connection with the nuclear file, in fact, applies more broadly. Engaging in a diplomatic process on the broad range of issues at stake between our two states and working toward the restoration of Iran’s relationship with the international community would offer clear benefits for Iran and the Iranian people. But equally so, any continuation on its present course will entail high and increasing costs for Iran. Putting that choice to the Iranian leadership as clearly and acutely as possible is the core of our policy.

What we seek, let me emphasize, is a change in Iran’s behavior--a change in how it assesses and interacts within its own strategic environment. We should not let the Iranian leadership entrench itself on the false pretext that it is under threat from the outside. We have committed repeatedly and at the highest levels to deal diplomatically with the Iranian regime. The fact that this diplomatic dialogue has been limited to less than satisfying talks in Baghdad is the unfortunate

choice of the Iranian leadership. As the recent presentation of yet another P5+1 offer makes clear, we do not exclude engagement. We remain ready to talk to Tehran about its nuclear program and the array of other American concerns about Iranian policies, as well as to address any issues Iran chooses to raise in a diplomatic context.

The Iranians are not completely closed off, and neither should the United States be. Careful consideration suggests that in certain contexts, we should have overlapping interests with Iran – for example, in a stable, unified Iraq at peace with its neighbors, in a stable Afghanistan, and in stemming narcotics trafficking. Broadly speaking, a responsible Iran can and should play an important, positive role in the region. This is possible, if Iran is willing to work constructively with the international community and its neighbors.

We recognize that we have not yet achieved our desired goals: Iran has still not agreed to suspend uranium enrichment and other proliferation sensitive nuclear activities. Iran has not ceased unconventional warfare and some of its policies continue to contribute to regional instability. Iran's current leadership may be so dogmatic or paralyzed by internal disagreements that it cannot agree in the near-term to terms so obviously to its advantage. With our long-term goal of persuading Iran to change its current course in mind, our immediate actions are intended to clarify the price of defiance by forcing Tehran to find new finance and trade partners and replace funding streams it has lost. We have made several notable successes, and will continue to work toward the objective of triggering a strategic recalculation in Iran's thinking.