
IRAN: WHERE NEXT ON THE NUCLEAR STANDOFF?

I. OVERVIEW

On 15 November 2004, Iran and the EU-3 (France, Germany and the UK) signed a new agreement on the nuclear standoff, with Iran accepting more comprehensive suspension of uranium enrichment, and the Europeans dangling more detailed economic rewards. This will keep the matter from the Security Council for now and, like its predecessor agreement in 2003, is a positive step that could temporarily interrupt nuclear efforts. But at best it is only a prelude to more critical negotiations over long-term arrangements that must include the U.S.

One year ago, Crisis Group (ICG) called the deal between Iran and the Europeans a crisis deferred, because it did not address the underlying issues.¹ What little has changed since then is mainly for the worse: added mistrust, fewer options available and, critically, less time as the nuclear clock ticks. That deal collapsed, Iran's conservatives strengthened their hold, and the country has pursued its nuclear program. It is imperative that the U.S. become engaged in seeking a comprehensive resolution that also meets legitimate Iranian security interests.

Washington stayed on the sidelines, acquiescing in the deal but not believing in it, refusing to table incentives while warning Iran was moving closer to a bomb. It has two assumptions. First, the current regime is determined to develop a nuclear weapon, so the international community ought not to be fooled into a policy of engagement. Secondly, this problem can only be addressed by a new regime in Iran that either abandons the nuclear program or at least renders it far less threatening -- to offer the current regime diplomatic or economic incentives would only strengthen it and delay the necessary change.

There is some reason -- based on track records -- for such scepticism. Tehran plays the EU and International Atomic Energy Agency (IAEA) skilfully while acting as if it has something to hide. De facto violation of its commitment to suspend enrichment activity, production of significant amounts of uranium hexafluoride, and continued work on a heavy water reactor -- among other suspicious activities -- hardly inspires confidence. Leadership in Tehran that pursued different policies on issues such as support for violent groups or opposition to Arab-Israeli peace certainly would alleviate concerns and, given high popular dissatisfaction, eventual political change cannot entirely be ruled out. Finally, EU and other international players such as Russia or China often appear to give political and economic interests precedence over non-proliferation concerns. Still, the U.S. posture is self-defeating, for the following reasons:

- *With regard to the nuclear program*, if Iran is prepared to trade away military ambitions, only the U.S. can give it the political, economic or security compensation that it wants; and if Iran is not prepared to deal, then only rejection of a good faith U.S. offer will persuade the world. Nor should one assume Tehran's position is static, impervious to influence: dangling normalised relations with Washington could shape views within the regime and heighten costs of a military program for those who would benefit from expanded trade. Under either scenario, the U.S. must add its incentives to Europe's to achieve its objectives.
- *With regard to regime-change*, there is no assurance it will occur anytime soon. Events this year -- rout of the reformists in parliamentary elections; sharp rise in oil prices; U.S. difficulties in Iraq -- have bolstered hard-liners and raised regime confidence to the highest level in a decade. As reformists argue, Washington should exploit fault-lines within the regime, pitting those who favour economic liberalisation and trade against those who benefit from a closed economy. Instead, it is generating nationalistic

¹ ICG Middle East Report N°18, *Dealing with Iran's Nuclear Program*, 27 October 2003.

unity leading to the combination it should most try to avoid -- a regime hostile to U.S. interests and moving toward the bomb. In short, the nuclear clock is ticking at a faster and more reliable rate than the regime-change clock.

Nor has the U.S. offered a realistic alternative to EU-3 policy. Counter-proliferation efforts have mixed prospects at best. Iran's program appears sufficiently advanced as to be immune to sanctions. A pre-emptive U.S. or Israeli strike would carry great risk for uncertain gain.

The U.S. has threatened Iran for four years but offered no tangible incentives to change behaviour. It overestimated the ability of Iran's youth to foment political change, while underestimating the hardliners' capacity for political revival. It vocally pressed for regime change, thus boosting Iran's ambitions for a nuclear deterrent. The second Bush administration will need to confront rapidly the issue it so far has studiously avoided. This is what needs to happen:

- *Iran must immediately and unconditionally implement its new agreement with the EU-3, in particular suspending uranium enrichment activities.*
- *Once the IAEA has verified Iranian implementation, negotiations on longer-term arrangements should begin.* For these to have any chance, the U.S. will need to back EU incentives with its own. Iran has legitimate economic, political and security concerns. Assuming it would forsake a military program, it will only do so if these will be met. Enhanced integration in the world economy (e.g., through the WTO) would exacerbate latent divisions within the regime, strengthen pragmatic voices, and heighten the opportunity costs of a military program. Ideally, Iran would permanently forego the right to an indigenous fuel cycle, but if it is in compliance with the Nuclear Non-proliferation Treaty (NPT) and Additional Protocol requirements, the West may have to settle for less. Joint Iranian/international management of its nuclear facilities -- not required under the NPT -- should be considered an acceptable compromise.
- *If Iran rejects a comprehensive good faith offer, a plan of graduated sanctions will be needed.* In order to persuade the U.S. to go down the diplomatic path, the EU and others -- China, Russia and Japan -- should commit upfront to such sanctions -- preferably backed by a Security Council resolution -- in the event negotiations fail.

II. NUCLEAR UPDATE

A. THE RISE AND FALL OF THE FIRST EU-3 DEAL

In October 2003, Iran reached agreement with France, Germany and the UK pursuant to which it committed to:

- "engage in full co-operation with the IAEA to address and resolve through full transparency all requirements and outstanding issues of the Agency and clarify and correct any possible failures and deficiencies within the IAEA";
- "sign the IAEA Additional Protocol and commence ratification procedures";
- "continue to cooperate with the Agency in accordance with the Protocol in advance of its ratification"; and
- "voluntarily . . . suspend all uranium enrichment and reprocessing activities as defined by the IAEA".

In return, the EU-3 stated that "this will open the way to a dialogue on a basis for longer-term cooperation. In particular, once international concerns . . . are fully resolved Iran could expect easier access to modern technology and supplies in a range of areas".²

Initial steps were promising. Iran announced it was suspending uranium enrichment, acknowledged past activities indicating it had been developing a uranium enrichment capability using centrifuges for eighteen years and a laser enrichment program for twelve, and granted IAEA inspectors greater access to its sites.³

On 18 December 2003, it signed the Additional Protocols. Mohamed ElBaradei, the IAEA director general, remarked: "If you look at the big picture, we are clearly moving in the right direction. If you

² "Iran Declaration", available at http://news.bbc.co.uk/1/hi/world/middle_east/3211036.

³ Iran also admitted to using small amounts of uranium hexafluoride to test centrifuges at the Kalaye Electric Company. It had previously acknowledged producing centrifuge components there but had denied conducting any tests with nuclear material. Paul Kerr, "The IAEA's Report on Iran: An Analysis", Arms Control Association, December 2003.

compare where we were a year ago and where we are today, that's a sea change".⁴

But that EU deal is now virtually dead. IAEA concerns focus on three principal issues:

- *Absence of full cooperation:* Iran began to drag its feet on some inspections, particularly those concerning military sites; because agreement was not reached on access to facilities controlled by the Defence Industries Organisation, the IAEA could not effectively verify the cessation of centrifuge construction. Discrepancies and gaps in Iran's declarations also surfaced, as did the familiar pattern of it being confronted with new evidence of undeclared activities and offering incomplete and shifting explanations in response.
- *Possible concealment of advanced centrifuge designs:* IAEA investigations of Tehran's declarations led it to suspect that Iran had hidden more advanced centrifuge designs.⁵ Eventually, after further questioning, Iran acknowledged that it had received P-2 centrifuge drawings from foreign sources in 1994 and had conducted some mechanical tests using non-nuclear material.⁶ But it offered changing and unconvincing rationales for its earlier reporting failure, which the IAEA called "a serious matter".
- *Presence of enriched uranium:* IAEA environmental sample tests of nuclear equipment showed traces of low-enriched uranium. Iran claimed that they originated from imported centrifuge equipment, and subsequent information pointed to Pakistani scientist A.Q. Khan, the "father" of his country's nuclear bomb, as the likely source. But "the confirmation was only

possible after Islamabad gave the IAEA data to verify the uranium source, and the U.S. provided a simulation of the Pakistani nuclear program that matched the account".⁷ Iran, in other words, had little to do with proving its case. More significantly, the IAEA found differing levels of enriched uranium contamination at nuclear facilities, raising the possibility -- though not more than that -- that some enrichment had occurred indigenously.⁸

The presence of low-enriched uranium was significant in that it suggested Iran may possess technical mastery of the entire nuclear fuel cycle, a critical threshold after which international non-proliferation measures cease to be adequate. Once various engineering problems are resolved and requisite industrial capacity is built (both of which could consume significant time), Tehran would have the ability to produce nuclear weapons.⁹

In January 2004, Iranian officials also stated that they were continuing to assemble centrifuges using components held in inventory -- an apparent violation of the spirit, if not the letter, of the EU agreement, which spoke of the suspension of uranium enrichment "activities". And in April, Iran advised the IAEA of its intention to proceed with tests on the production of uranium hexafluoride (the feedstock for enriched uranium).¹⁰

Tensions came to a head in June 2004 when the IAEA criticised Iran for not cooperating fully, particularly with regard to advanced centrifuge activity and production of plutonium. Even European countries eager to preserve the deal had harsh words for Iran, which they accused of renegeing on its essential

⁴ Quoted in Reuters, 2 March 2004.

⁵ The IAEA suspected that Iran had designs for the P-2 centrifuge. Like the less refined P-1, the P-2 centrifuge is an early European design that more efficiently produces enriched uranium.

⁶ The designs in question were essentially the same as those stolen from a Dutch nuclear research facility by Pakistani scientist A.Q. Khan in 1974 and sold to Libya. (Khan was tried *in absentia* and found guilty for this theft in a Dutch court; his conviction was subsequently overturned on procedural grounds).

See "A.Q. Khan", at www.globalsecurity.org/wmd/world/pakistan/khan.htm. Iran insisted that it had not purchased P-2 centrifuges abroad, and that what components it had, it had manufactured domestically. See "Nuclear Weapons - 2004 Developments", available at www.globalsecurity.org/wmd/world/iran/nuke2004.htm.

⁷ Policy Brief #2, from an 8 March 2002 Congressional Staff briefing on "U.S. Challenges and Choices in the Gulf: Iran".

⁸ Uranium contamination found at the Kalaye Electric Company differed from that found at the Natanz facility even though Iran claimed contamination in both cases came from imported centrifuge components.

⁹ It is worth noting that the dismantling and suppression of the A.Q. Khan network, although incomplete, likely has removed an important source for Iran's nuclear program.

¹⁰ In response to IAEA concern that production in the amounts indicated -- almost 100 kilograms -- was tantamount to producing feed material for enrichment, Iran claimed that "the decision taken for voluntary and temporary suspension is based on clearly defined scope which does not include suspension of production of UF₆ (uranium hexafluoride). IAEA, "Implementation of the NPT Safeguards Agreement in the Islamic Republic of Iran", Report by the Director General, GOV/2004/27, 1 June 2004.

components.¹¹ For its part, Iran blamed the EU-3 for not living up to their side by failing to provide Tehran with nuclear technology and by supporting critical IAEA resolutions.¹² On 24 June 2004, Iran formally notified them it would resume manufacturing parts for uranium centrifuges and conduct conversion experiments to produce uranium hexafluoride, albeit under IAEA supervision.¹³ The 2003 agreement was, for all intents and purposes, void.¹⁴

B. THE IAEA RESPONSE

At its 18 September 2004 meeting, the IAEA acknowledged that the picture remained ambiguous and that it could not "draw definitive conclusions concerning the correctness and completeness of Iran's declarations". While not uncovering a smoking gun, it nonetheless faulted Iran for its failure to suspend all enrichment related and reprocessing activities, called for parliamentary ratification of the Additional Protocol, reconsideration of the decision to build a heavy water reactor, prompt access to sites, and explanations regarding why varying degrees of enriched uranium contamination had been found. It called on Tehran to promote confidence by "immediately suspend[ing] all enrichment related activities, including the manufacture or import of centrifuge components, the assembly and testing of centrifuges, and the provision of feed material, including through tests or production".¹⁵

¹¹ Crisis Group interviews with German and French officials, Tehran, Paris, and Washington, February-March 2004.

¹² The Iranian argument is not very convincing as the agreement states that Iran must first take its confidence-building steps before Europe will provide greater technological access.

¹³ Discussions as to what such supervision would involve are ongoing. Iran has not agreed to suggestions that completed centrifuges be sealed by the IAEA. "Implementation of the NPT Safeguards Agreement in the Islamic Republic of Iran", Report by the Director General, GOV/2004/60, 1 September 2004. In a joint statement, the U.S. and the EU expressed their concern about Iran's intention to resume the manufacture and assembly of centrifuge components. U.S. Undersecretary of State for Arms Control and International Security John Bolton referred to an "act of defiance of the IAEA board of governors" and "a thumb in the eye of the international community". IPS, 29 June 2004.

¹⁴ I. Traynor, "Iran to Resume Nuclear Programme", *The Guardian*, 28 June 2004. Available at www.guardian.co.uk/iran/story/0,12858,1248785,00.html.

¹⁵ IAEA, "Implementation of the NPT Safeguards Agreement in the Islamic Republic of Iran", Resolution Adopted By the Board on 18 September 2004, GOV/2004/79, 18 September 2004.

Despite U.S. pressure, the IAEA declined to take matters further, in particular to refer the case to the UN Security Council (UNSC). Deferring matters, it instead concluded that it would decide at its 25 November meeting whether "further steps are appropriate in relation to Iran's obligation under its NPT [Nuclear Non-Proliferation Treaty] Safeguards Agreement [and] the requests made of Iran, as confidence building measures, by the Board in this and previous resolutions".¹⁶ In other words, it gave Iran until the end of November to suspend all uranium enrichment activities, mothball its heavy water plutonium plant, and ratify the Additional Protocol or face unspecified action, almost certainly renewed U.S. efforts to bring the matter to the Security Council.

Its latest report, issued on 15 November again drew a mixed picture, detailing areas still under investigation (principally the provenance of the enriched uranium and the extent of Iran's efforts to obtain centrifuges) and Iran's failures to report or declare activities. It concluded that "Iran has made substantial efforts over the past two decades to master an independent nuclear fuel cycle and...conducted experiments to acquire the know-how for almost every aspect of the fuel cycle", and that it was "not yet in a position to conclude that there are no undeclared materials or activities in Iran".¹⁷

C. THE NEW AGREEMENT

As they faced the 25 November 2004 deadline, the EU-3 appeared both exasperated by Iran's behaviour and frustrated with the U.S. refusal to engage.¹⁸ Their diagnosis was that Tehran was determined to keep the nuclear option alive, possibly until such time as it could extract concessions from Washington, possibly forever. With elections in the U.S. only weeks away, any hope for a new American approach capable of testing and altering Iranian calculations prior to the IAEA meeting faded. Seeking at the very least to buy time and avoid a UNSC referral from which they could envisage little benefit -- and, possibly, considerable harm, including Iran's withdrawal from the NPT -- the Europeans presented Iran with a new offer on 21 October.

¹⁶ BBC, 18 September 2004.

¹⁷ IAEA, "Implementation of the NPT Safeguards Agreement in the Islamic Republic of Iran", 15 November 2004.

¹⁸ Crisis Group interview with EU-3 diplomat, Washington, September 2004.

Though modelled after the 2003 proposal, it addressed the previous proposal's lack of specificity, providing much greater clarity regarding the scope of both Iran's commitments and Europe's incentives. This way it hoped to receive more explicit U.S. backing.¹⁹ In essence, the EU would provide Iran with a guaranteed nuclear power fuel supply and civilian nuclear technology -- including possibly a light water research facility -- once Iran had demonstrated it was not seeking nuclear weapons. In addition, the EU proposed far-ranging economic assistance, increased trade and support for Tehran's efforts to join the World Trade Organisation (WTO). In exchange, Iran would have to suspend indefinitely its fuel enrichment activities and relinquish its plutonium production capacity by halting the construction of a heavy water reactor. If Iran rejected the proposal, the Europeans intimated they were prepared to endorse a series of incremental sanctions, either through the UN or -- were that to prove impossible, as seemed likely -- a group of like-minded nations.

Iran's reaction followed a familiar pattern, relatively positive responses alternating with clearly negative ones -- stringing out negotiations, awaiting the arrival of a new U.S. administration, while making clear that without modification the proposal would ultimately not fly. Iran took the position that a deal with Europe was possible, that it would accept measures designed to reassure the international community over its military intentions, but that it reserved the right to an indigenous fuel-cycle capacity -- the last item a direct contradiction of the European proposal.

While Iranian officials described the offer as "unbalanced," they also emphasised that negotiations should continue and a compromise was "achievable."²⁰ The goal, they said, was to "reach a balanced agreement, one that would eliminate Europeans' worries...and one that would recognise our rights within the non-proliferation treaty [i.e., to possess an indigenous enrichment capacity]".²¹ Supreme Leader Ayatollah Khamenei said Iran would pull out of negotiations if indefinite suspension of uranium enrichment remained a demand,²² and Hashemi Rafsanjani, the former president and current head of the influential Expediency Council, warned that while Iran "agrees to continue

negotiations within the framework of international rules, if the Europeans want to use threats, there is no more place for negotiations".²³ Explaining Tehran's position, Hossein Mousavian, the top Iranian negotiator, stated that it "cannot rely on the fuel the Europeans are offering, because they might withdraw it any time there are differences in relations. We need to become independent in providing our own fuel".²⁴ Adding to the confusion, Iran's parliament on 31 October unanimously approved a bill that called for the resumption of uranium enrichment -- a move almost certainly intended to strengthen the hand of Iranian negotiators in Paris.²⁵

Following additional negotiations, on 15 November 2004 Iran and the EU-3 announced their new agreement. Its main elements included:

- ❑ Iran's affirmation that it did not and would not seek to acquire nuclear weapons;
- ❑ Iran's commitment to continue implementing the Additional Protocol pending its ratification -- a prospect made more difficult by its parliament's position;
- ❑ Iran's voluntary suspension of "all enrichment related and reprocessing activities". Unlike the 2003 agreement, this version went on to describe such activities comprehensively and in detail, to include "the manufacture and import of gas centrifuges and their components, the assembly, installation, testing or operation of gas centrifuges, work to undertake any plutonium separation, or to construct or operate any plutonium separation installation, and all tests or production at any uranium conversion installation".
- ❑ Once the IAEA has verified this suspension (in time for its 25 November meeting), negotiations between Iran and the EU will begin over a longer-term agreement under which Iran would provide guarantees (to be defined) that its program is exclusively for peaceful purposes and Europe would offer expanded trade and economic cooperation (such as conclusion of the Trade and Cooperation Agreement with the EU and support for WTO accession), civilian nuclear cooperation

¹⁹ Crisis Group interview with German official, Washington, October 2004.

²⁰ Eurasia Net, 25 October 2004.

²¹ Foreign Ministry spokesman quoted in *The New York Times*, 25 October 2004.

²² Associated Press, 28 October 2004.

²³ IRNA, 29 October 2004

²⁴ Hossein Mousavian, in *The New York Times*, 25 October 2004.

²⁵ The vote was only for the outline of the bill; it carried no legislative weight, and the EU treated it as such.

(such as provision of a light water reactor) and security guarantees.

On 22 November, three days before the IAEA meeting, ElBaradei announced that Iran had apparently frozen its nuclear activities, stating: "I think pretty much everything has come to a halt right now".²⁶ But the run-up to the announcement was indicative of the fragility of the deal and of the rough road that lies ahead: an exiled opposition group, the National Council for Resistance in Iran (NCRI), accused Iran of running a secret uranium enrichment program; on 17 November, U.S. Secretary of State Colin Powell charged that Iran was developing missiles capable of carrying nuclear warheads; and reports surfaced that Iran was racing to produce uranium hexafluoride during the period immediately preceding the suspension. On the eve of the IAEA meeting, EU-3 and Iranian negotiators continued to labour over detailed wording with both sides indicating that failure remained possible.²⁷

Ultimately, as both Iran and the EU are quick to acknowledge, though not for the same reasons, the agreement is a step forward that still leaves important issues unresolved, in particular regarding the duration of the suspension of enrichment activities. With the EU calling for an indefinite suspension, and Iran insisting that it be time-bound, the compromise solution was to tie its duration to negotiations over a long-term agreement. But the fundamental gap remains.

For now, however, EU officials argue that there is no better alternative. With neither regime change nor military action as a realistic option, seeking to slow down the Iranian program and trying to affect the cost-benefit assessment of leaders whose primary goal is regime survival, appears to them by far the wisest course.²⁸ They hope to play on -- and deepen -- presumed differences within the regime and strengthen those who favour negotiations and compliance with the NPT by offering the prospect of economic and eventually political and security benefits. Meanwhile, and in the short run, Iran's commitments and more intrusive IAEA inspections

heighten the cost to Tehran of non-compliance. EU officials also claim that in the event of Iranian breach, they will be prepared to support UNSC action and, in the event of a Russian or Chinese veto, undertake joint action with the U.S.²⁹ "We will take this immediately to the UNSC if they renege on this agreement", an EU diplomat asserted. "We were only a few days away from taking it to the UNSC this time".³⁰

As a senior official from one of the three EU countries put it:

We are not naïve and understand Washington's scepticism. But what else should we do? We at least are doing something that will halt Iran's program and give us time to explore the possibility of a deal. If we succeed, we all will come out ahead. If it fails, Iran's violations will be that much more obvious and we will be in a stronger position to rally support for sanctions.³¹

In order for this approach to have a chance of succeeding, they emphasise, the U.S. will have to change its policy for, although the EU can offer some incentives, only America's have a chance of closing the deal.

The EU will find it difficult to offer adequate civilian technological assistance -- for instance a light water reactor -- without U.S. approval. And at the end of the day, it is U.S. economic ties and political and security guarantees that Iran is after. The only true test of Iran's intentions will come if the U.S. is part of the incentive package.³²

In the short term, EU officials emphasise, the burden will be on Iran truly and comprehensively to suspend its enrichment activities and allow inspections. But the burden will then be on Washington to show greater flexibility than so far has been the case. "We have two principal fears: that Iran not play ball now, and that Washington not play ball later".³³

²⁶ *The New York Times*, 23 November 2004.

²⁷ See for example, Christopher Adams, "Nuclear Talks between Iran and EU states hit hurdle", *Financial Times*, 24 November 2004. "We have 48 hours of hard work to do", a senior British official said. "It is close to being done, but not there yet".

²⁸ Crisis Group interviews with EU officials, Paris/Brussels, November 2004.

²⁹ *Ibid.*

³⁰ Crisis Group interview, Tehran, 18 November 2004

³¹ Crisis Group interview, November 2004.

³² Crisis Group interview with EU official, November 2004.

³³ Crisis Group interview with European official, November 2004.

III. DEVELOPMENTS IN IRAN

A. POLITICAL DEVELOPMENTS

That conservative candidates swept the February 2004 parliamentary elections was hardly a surprise. Most reformist candidates were either barred by the Islamic Guardian Council or boycotted in protest.³⁴ A disillusioned public had vowed to shun the polls long before the reformist boycott.³⁵ As a result, the tug of war no longer opposes conservatives and reformists; essentially, it has become an intra-conservative one.

Because the victorious conservatives ran on a platform of economic change and development, most analysts assumed they belonged to the pragmatic wing of the conservative camp. Indeed, in October 2003, Crisis Group assessed that "Iranians may...settle by default for modest changes through a new breed of pragmatic conservatism inspired by former President Rafsanjani", and that this could translate into a mix of economic liberalisation, political repression, gradual cultural loosening and, on the diplomatic front, "a conciliatory foreign policy that helps inoculate the regime from international criticism and promote foreign investment".³⁶

The prognosis appears to have been overly optimistic. Since the new parliament assumed control in June 2004, it has taken a noticeable rightward shift. Talk of a "China model", once prevalent, no longer is in vogue: many parliamentarians oppose both political liberalisation and socio-economic reform, pushing a populist-Islamist agenda and seeking to undo social and political changes, while at the same time railing against foreign investment and privatisation. Rhetorically at least, Iran's diplomacy has harkened back to the more radical pronouncements of the pre-Khatami period.

Referred to as the *Abadgaran* (Developers of Islamic Iran), or "new conservatives", these members of parliament in many ways are distinct from both

Khamenei-style traditionalists and Rafsanjani-style pragmatists. Whereas revolutionary fervour among old-guard conservatives has waned over the years, the relatively young and politically inexperienced *Abadgaran* seem a throwback to the revolution's early years, espousing Islamic values, populist economic policies, and, regionally, a more active, anti-American foreign policy. Many *Abadgaran* members are former revolutionary guardsmen, and they continue to enjoy a close relationship with the Iranian Revolutionary Guard Corps (IRGC).³⁷

In this, however, the parliament may be less cause than symptom. Domestic and regional developments have contributed to what several Iranian observers refer to as a militarisation of politics, with hard-line factions and groups that operate independently of elected institutions being elevated to key economic and political positions.³⁸ As an Iranian reformist put it, the more polarised the regional situation and the more security is perceived as the overriding concern, the greater the likelihood that various factions will close ranks around hard-line positions.³⁹ The growing sense of national encirclement has importantly advanced the position of the IRGC and powerful religious foundations (*bonyads*),⁴⁰ which benefit from political and economic monopolies, are served by a closed and isolated economy, and would be hurt by expanded, liberalised trade.

Of particular note is the role of the IRGC. Former revolutionary guardsmen include Tehran's new mayor, the newly appointed head of the country's broadcast monopoly, *Sedah va Sima*, and at least several dozen of Iran's 290 *Majles* deputies; the IRGC's decision-making influence is widely believed to have been enhanced; and its role is increasingly mentioned in connection with the nuclear program, activities in Iraq, relations with the U.S., and domestic policies.⁴¹ Though couched in ideological terms, the

³⁴ The Guardian Council is a highly conservative, unelected twelve-member body that has the authority to veto parliamentary decisions and vet political candidates. It is largely aligned with Supreme Leader Khamenei, as he appoints half of the members. For more on the Council, see ICG Middle East Report N°5, *Iran: The Struggle for the Revolution's Soul*, August 5 2002.

³⁵ See ICG Middle East Briefing, *Iran: Discontent and Disarray*, 15 October 2003.

³⁶ *Ibid.*

³⁷ For a more in-depth look at the *Abadgaran*, see Kamal Yazin, "Iranian neo-cons make power play in Tehran", Eurasianet.org, 1 October 2004.

³⁸ Crisis Group interview with Mahmoud Sariolghalam, Iranian policy analyst and professor, Tehran, 25 August 2004.

³⁹ Crisis Group interview with Ali Reza Alavi-Tabar, Tehran, 25 September 2004.

⁴⁰ *Bonyads* are not accountable to any branch of the state but are overseen by the Supreme Leader through his representatives. They are not mentioned in the constitution.

⁴¹ In a 1 September 2004 speech to reformist politicians entitled "The phenomena of militarisation", influential reformist thinker Ali Reza Alavi-Tabar cited the prevalence of military forces in the decision making process and the

IRGC's political stance appears to a considerable extent motivated by economic interests. An importer-exporter of industrial items claimed:

Many of them don't want to see the country open up. They fear that in a different system the competition from people with proper education and expertise could end their racket. This is not about ideology ... they have serious financial interests at stake.⁴²

Front companies controlled by the IRGC are increasingly active in major sectors of the economy, notably telecommunications. They also are widely believed to control more than 70 ports around the country, earning billions of dollars from tax-free imports and exports, including the smuggling of contraband.⁴³ An incident illustrating the IRGC's increased stake in economic/political decisions as well as its enhanced status was its June 2004 closure of the newly-constructed Imam Khomeini International Airport (IKIA), after only a single flight had occurred. The fact that the airport, meant to be one of the few showcases of the Khatami government, was to be operated by a Turkish-Austrian consortium and not a local firm ostensibly provoked their outrage. But as a diplomat remarked: "There are two reasons why the IRGC closed the IKIA. First, to send a signal to the president, telling him, 'behave yourself', and secondly, for their own business interests".⁴⁴ More generally, the relationship between Ayatollah Khamenei and the IRGC is seen as becoming increasingly symbiotic, politically expedient

priority given to military and paramilitary entities in domestic affairs. He argued that this was an unprecedented phenomenon that did not exist even in the challenging days after the Iran-Iraq war.

⁴² Crisis Group interview, Tehran, October 2004.

⁴³ "The Revolutionary Guards are back", *The Economist*, 17 June 2004.

⁴⁴ Crisis Group interview, Tehran, 11 August 2004. In a statement, the IRGC explained: "The airport will remain closed until security requirements are met". Iran Air had subcontracted operation of the airport to a Turkish-Austrian consortium but the armed forces objected this jeopardised the country's "security" and "dignity". "Regretfully, officials of the airport have taken this inappropriate decision without heeding security requirements as well as the law of the Supreme National Security Council on not using foreign forces", they asserted. See, Reuters 3 February 2004; IRNA 11 May 2004. Diplomats, political activists and regional managers of oil consortia working in Iran read this as a sign of the IRGC's growing claim to influence policy decisions and growing involvement in economic areas. Crisis Group interviews, August/September 2004.

for the leader and economically expedient for the *pasdaran*.⁴⁵

Having assumed control of most elected and unelected institutional power bases, the conservative wing is now awaiting presidential elections in May 2005 to fully consolidate its position.⁴⁶ In the meantime, observers tend to agree that the Islamic Republic is "more stable, more repressive and less amenable to foreign pressure than it has been in over a decade".⁴⁷ As Abbas Milani, an Iranian analyst, insightfully observed, a string of policy failures by the U.S. and Iran's opposition contributed to this remarkable outcome: a regime that came to power invoking divine sovereignty and embracing pan-Islamism has managed to refashion itself as the standard bearer of popular sovereignty and nationalism.⁴⁸

B. IMPACT ON NUCLEAR DEBATE

As described in Crisis Group's earlier report, three broad characteristics mark the internal debate:

- A widespread consensus that Iran has the right to develop a peaceful nuclear energy program, including the right to possess an indigenous uranium enrichment capacity. The nuclear program "has become a 'national project,' a source of pride that no decision maker, whether reformist or conservative, c[an] abandon".⁴⁹ Indeed, even reformists frame their arguments for a more flexible approach to the international community in terms of what is most likely to protect this right.

⁴⁵ "When we're trying to launch an initiative, it usually clears the various branches of government, but once it reaches the IRGC we often run into problems or are blocked. It shows where power has shifted". Crisis Group interview with UN official, Tehran, November 2004.

⁴⁶ In addition to former President Hashemi Rafsanjani, potential conservative candidates include former foreign minister Aliakbar Velayati -- a close advisor to Khamenei -- and a number of *Abadgaran* or "new conservatives".

⁴⁷ Gareth Evans and Karim Sadjadpour, "Iraq chaos has only emboldened Iran", *International Herald Tribune*, 12 October 2004.

⁴⁸ Abbas Milani at Carnegie Endowment conference, Washington, 5 November 2004.

⁴⁹ ICG Report, *Dealing with Iran's Nuclear Program*, op. cit., p. 16. President Khatami said of Iran's nuclear program: "This is our national interest and prestige. This is our strategy. But if they want to deny us our basic right [to develop a peaceful nuclear program], we and our nation have to be prepared to pay the price". Associated Press, 17 August 2004.

The president's brother and former parliamentarian Mohammadreza Khatami explained:

When we were in the (sixth) parliament, confidence building with the help of the government was manifested in stopping the fuel cycle. We believe if that trend had continued, the suspension of the fuel cycle would have been temporary. Eventually we would have been able to keep our fuel cycle. But under the current circumstances..., because of the international political and economic pressures and the lack of trust, that is impossible. Such ambitions today will only bring infightings and tension.⁵⁰

- A fragile agreement on the wisdom of cooperating with the IAEA and EU in order to avoid referral to the UNSC and further diplomatic isolation.
- An unfinished debate over whether Iran ought to pursue a military nuclear program, with proponents principally invoking regional and international threat perceptions and Iran's national pride. The precedent of Pakistan and India (where brief international indignation was quickly followed by acquiescence in their nuclear status) did not go unnoticed, and Iranian officials are said to consult closely with Indian counterparts.⁵¹ A U.S. official acknowledged, "even among Iranians eager for relations with the U.S., the Indian example weighs heavily: it developed a bomb, and two years later we were talking".⁵² Tehran also observed the fall of the Baathist regime in Iraq (which did not develop a nuclear deterrent) and the continued survival of the regime in Pyongyang (which apparently did).⁵³ For now, Iran's policy appears to be to keep all options open; it has yet to signal a bottom line on the military question and, as a

U.S. official remarked, "may not even know what it is at this point".⁵⁴

Given Iran's opaque political system, it is difficult to assess the precise extent to which developments over the last year have affected its nuclear policy. Major foreign policy decisions -- notably on the nuclear file -- are made by a small group of high-level officials who arguably are insulated from electoral shifts or changes in formal institutional structures.⁵⁵ Still, there appears to have been an interplay of domestic and international events, with the strengthening of the conservative factions, toughening the nuclear posture and, in turn, polarisation over the nuclear issue coupled with anxiety over U.S. policy helping solidify the hardliners' hold.

While neither body is a prime decision-maker on foreign policy or security matters, the IRGC's conduct in the airport incident and the *Majles*' harsh tone on the nuclear question are indicative of a radicalised domestic climate in a system that, although not democratic, operates with pluralistic bases of power and influence. By affecting public opinion and through formal or informal lobbying, mass demonstrations, *basij* or IRGC gatherings, Friday prayers and media pronouncements⁵⁶ also help shape the balance of power and, indirectly, policy decisions. The IRGC is seen as playing a more important role in the foreign policy and nuclear debates, tilting them toward those who

⁵⁰ Crisis Group interview with Mohammadreza Khatami, Tehran, 2 October 2004.

⁵¹ Crisis Group interview with U.S. official, Washington, October 2004.

⁵² Ibid.

⁵³ U.S. officials have validated this perception by their differentiated treatment of Iran and North Korea. Pressure on Tehran was justified by a U.S. official on the ground that it had not yet produced a weapon. "We're past that point with North Korea", he said. Quoted in the *The New York Times*, 21 November 2004.

⁵⁴ Ibid.

⁵⁵ ICG Report, *Dealing with Iran's Nuclear Program*, op. cit., p. 20.

⁵⁶ There are several influential conservative newspapers. Political activists appear most worried about being targeted by *Keyhan* and its editor in chief, Hossein Shariatmadari, who was appointed by the Supreme Leader as head of the paper and the institution that bears the same name. According to former Deputy Foreign Minister Abbas Maleki, "*Keyhan* defends revolutionary values....*Keyhan* characteristically takes a critical view on everything. When asked why, he [Shariatmadari] says criticism makes the decision makers think twice before acting. This forces them to consider more carefully the consequences of their decisions". Crisis Group interview with Maleki, Tehran, August 2004. *Keyhan* has argued in favour of Iran's withdrawal from the NPT; as Shariatmadari explained, "We shall no doubt reach the point where in order to safeguard our sovereignty and interests, exit from the NPT will present itself as the only logical and legal choice, a decision we should have made much earlier. It is not too late....Fortunately, the fundamentalist seventh *Majles* is determined not to approve the Additional Protocol and one might hope that it will also consider getting Iran out of the NPT". IPS, 29 June 2004.

view nuclear weapons as essential to boost the country's defensive capabilities.⁵⁷

Again, while not being determinative -- and while it probably suits the regime to have a more hard-line voice to show the Europeans the constraints it faces -- the *Majles'* sharp turn to the right has coloured the nuclear debate. On 10 August 2004, the new parliament strongly denounced Foreign Minister Kharrazi for "mishandling" of the nuclear dossier, "surrendering to the demands of the Europeans and the West".⁵⁸ A month later, after the IAEA passed a resolution against Iran, the parliament announced it would not ratify the Additional Protocol.⁵⁹ And, in the wake of the November 2004 agreement with the EU, parliamentarians were quick to voice objections. In the words of a hard-line member, Ahmad Tavakoli, "we agreed to make thirteen precise commitments while the Europeans only made four vague ones".⁶⁰

More hard-line elements successfully played on the widespread domestic perception that Iran is victim of a double standard (with countries like India, Pakistan or Israel developing nuclear weapons while Iran is denied its rights under the NPT) and that the EU failed to live up to its part of the original deal (technological, economic and other benefits).⁶¹ The claim that Iran has a right to a peaceful nuclear

program and is being treated unfairly is one from which few, moderate or conservative, dare depart. As one pragmatic conservative put it:

There is a difference between [the conservatives'] and the reformists' position [towards the EU]. Whenever the EU stepped up pressure, the reformists became weaker. We are more pragmatic and have come to learn the game of power better than them.⁶²

Differences also affect negotiating styles.

We [the regime prior to Khatami] had a power...of which the reform camp deprived us. Today, we are reviving it. It consists of others not seeing us as rational actors. We should not be calculable and predictable to them. This is "simulated irrationalism". The U.S. could not mess with Imam [Khomeini] because, he was not calculable. Our foreign policy has become too rational in the 2 Khordad [Khatami's reform movement]...Saddam's fall was because he was calculable; they knew that even if he had WMD he would not dare use them.⁶³

Growing U.S. difficulties in Iraq have lessened fears of American action against Iran -- as an Iranian official put it, "the presence of 140,000 U.S. soldiers in Iraq is not an American asset; it is a liability for they offer us a target in the event we are attacked"⁶⁴ -- without lessening the feeling that the U.S. intends to destabilise the regime.⁶⁵ The regime is at once "emboldened" and "extremely mistrustful of U.S. intentions".⁶⁶ "Iran feels strengthened by chaos in Iraq, but threat perceptions remain; the regime still feels the U.S. is actively pursuing a regime change policy".⁶⁷

⁵⁷ Crisis Group interviews, Tehran, September-October 2004; Crisis Group interview with political activist close to IRGC. See also, "Who Calls the Shots in Iran's Foreign Policy Offensive", *Iran Focus*, July 2004. The IRGC's top leadership has made clear its continued opposition to improved ties with the U.S. Hassan Abbasi, considered one of its key ideologues, vowed to "burn the roots of the Anglo-Saxon race" and claimed that Iran's "missiles are now ready to hit their civilization". RFE/RL Iran report, 14 June 2004. That said, the IRGC's rank and file is widely credited with far more moderate views. "The upper echelon of the *pasdaran* and the *basij* are hardliners. But the rank and file are reformists in their thoughts ... most of them voted for Khatami". Crisis Group interview with Ali Reza Alavi-Tabar, a reformist leader and former deputy commander in the IRGC, Tehran, 25 September 2004. Former IRGC chief Mohsen Rezaii, a conservative pragmatist who has advocated rapprochement with the U.S., is still believed to command widespread respect among guardsmen.

⁵⁸ "Iranian conservatives grill FM over nuclear dossier", *Agence France-Presse*, 10 August 2004.

⁵⁹ *Shargh*, 8 September 2004, p.7.

⁶⁰ Quoted in *The New York Times*, 17 November 2004.

⁶¹ As an Iranian observer noted, "the more the nuclear issue is debated, the more Iranians get incensed at what they perceive as unfair international treatment. When Iran's need for nuclear power is questioned in light of its extensive oil and gas reserves, people say, 'then what about the U.S.?'". Crisis Group interview, Tehran, September 2004.

⁶² Crisis Group interview with Amir Mohebbian, a columnist at the conservative daily *Resalat*, Tehran, 23 September 2004. Viewed as a pragmatist, Mohebbian is closely associated with the traditional conservative Society of Islamic Engineers, at whose headquarters the interview took place.

⁶³ *Ibid.*

⁶⁴ Crisis Group interview, September 2004. "The U.S. needs to see the reality in Iran ... the idea of regime change is a joke". Crisis Group interview with former Deputy Foreign Minister Mahmoud Vaezi, Tehran, October 2004. Vaezi is an influential moderate conservative.

⁶⁵ Crisis Group interview with European diplomat, Tehran, October 2004.

⁶⁶ Crisis Group interview with EU diplomat, Tehran, October 2004.

⁶⁷ Crisis Group interview with Mahmoud Sariolghalam, Iranian policy analyst and professor, Tehran, 23 September 2004.

I accept they [Americans] are more powerful than us now, but the solution is not to give in. A state with all its armed forces is often powerless against insurgents and paramilitary forces, because a state has to defend its borders, while they need one man to disrupt something: A state, for example, needs to protect a line of, say 100 km., but an insurgent group needs to destroy only one metre of that....If they (Americans) step up pressure, we will do so too. With the nuclear issue things are going beyond their control....If it comes to a confrontation, the US will pay a dear price because the fight will not take place on Iranian soil. The whole region will fall apart. The calm in Afghanistan is partly due to Iran. In Iraq things can get worse. Even the relations between Israel, Syria and Lebanon are not unrelated to Iran.⁶⁸

To this one should add the significant impact of \$50/barrel oil prices,⁶⁹ which makes it far more difficult for Europe or even the U.S. to contemplate a crisis that could interrupt the flow of Iranian oil.⁷⁰ Aspirations to regional hegemony, in which a nuclear deterrent could play a pivotal part, also appear to have been revived. "Prior to 11 September there were three powers in the region", remarked Deputy Foreign Minister Vaezi. "Iraq has now been eliminated. Saudi Arabia is undergoing many difficulties....Iran has emerged as the strongest".⁷¹

In another indication of its current posture, Iran has begun issuing Shahab-3 missiles -- whose range is estimated at 810 miles -- to Revolutionary Guard units and has announced the successful testing of a version of the Shahab with a range of up to 1,250 miles. If stationed in northern Iran, such a missile would have the ability to reach as far as South East Europe.⁷²

⁶⁸ Crisis Group interview with Mohebbian, *op. cit.*

⁶⁹ All figures denoted in dollars (\$) in this report refer to U.S. dollars unless otherwise noted.

⁷⁰ According to Amir Mohebbian, "Neither the British nor the French will take our case to the [UN] Security Council. They have too many oil interests here". Crisis Group interview, Tehran, September 2004.

⁷¹ Crisis Group interview, Tehran, October 2004. Bijan Khajehpour, director of Atieh Bahar Consulting, added: "Iran is trying to project its power with the nuclear issue... if they're not going to be accepted in what they deem is their rightful role, they will impose themselves on the international community". Crisis Group interview, Tehran, November 2004.

⁷² In a military parade in September 2004, the IRGC emblazoned the new missile with the words "Death to Israel"

The agreement with the EU signals that Iran's basic calculus has not changed. The regime, although both more conservative and confident than in the past, continues to value economic and political ties with Europe. It also likely wishes to test whether and to what extent the U.S. is prepared to re-engage and how transatlantic relations evolve. All of which militates for an at least temporary cessation of its enrichment program. But arguments in favour of a military program remain and are being voiced by regime elements that have gained in strength. These elements also point to growing risks inherent in delay: that, as France and others have advocated, the NPT may be amended both to increase the cost of withdrawal and limit the scope of nuclear activity non-nuclear weapon states can legitimately engage in.⁷³ There is strong suspicion in Tehran that the amendments -- presented as of universal applicability -- would in the first instance target Iran, increasing the incentive to move fast on the nuclear front before the penalties become any higher.

As an insurance policy against a potential referral to the UNSC, Iran also has been diversifying its economic ties, targeting in particular permanent members of the Council, such as China and Russia. Tehran and Beijing recently signed a \$70 billion oil and light natural gas agreement pursuant to which China will purchase 250 million tons of natural gas over the next 25 years while the Chinese Sinopec Group will develop Iran's Yadavaran field.⁷⁴

and "Death to America". It is unknown how Iran may have extended the range of the missile, but possible means include more powerful fuel, giving higher initial velocities; lighter payloads; or redesigned engines permitting a longer burn time. P. Hafezi, "Iran says its missiles can now reach 1,250 miles", Reuters, 5 October 2004.

⁷³ The French proposal was presented at the preparatory committee for the 2005 review conference on the NPT. It would, *inter alia*, strengthen safeguards on the export of sensitive technologies, put forward a set of conditions (energy need, non-proliferation commitments) that need to be met for the export of such materials and impose penalties on countries that withdraw from the NPT (in particular, nuclear materials acquired in a third country prior to withdrawal would have to be returned to the supplying state, frozen or dismantled). Proposals put forward by Eibaradei would restrict civilian nuclear activity with potential military use "exclusively to facilities under multinational control". Also see ICG Report, *Dealing with Iran's Nuclear Program, op. cit.*, p. 33.

⁷⁴ See *The Washington Post*, 17 November 2004.

IV. WHAT THE U.S. AND ISRAEL MIGHT DO

A. UNITED STATES

For the past four years, the U.S. administration has been deeply divided -- and virtually paralysed -- over its Iran policy. The result has been agreement on the least common denominator: an almost exclusive focus on the nuclear issue -- the reality and urgency of which all agencies could agree on -- to the detriment of much else.⁷⁵

Most recently, absorbed by the presidential campaign and still bereft of a comprehensive policy, Washington adopted a relatively passive attitude, reluctantly and sceptically acquiescing in the EU initiative.⁷⁶ The U.S. blessing -- conveyed during a 15 October 2004 meeting between Under Secretary of State John Bolton and G-8 countries in a performance described by participants as "icy" and "hostile"⁷⁷-- was accompanied by considerable disdain for the diplomatic manoeuvre. In essence, Bolton made plain that he did not believe in the deal, but that the EU should feel free to proceed. Reflecting the dominant view in Washington, a U.S. official commented: "Iran will find a way to accommodate the EU offer, while leaving all options open -- in other words, it will agree to a suspension that is voluntary, time-bound and reversible".⁷⁸ Besides, with only days to go before the elections, Washington was hardly in a position to offer a counter-proposal.⁷⁹

Underneath, the basic U.S. position remains unaltered: First, Iran is moving steadily to develop a nuclear bomb under cover of a civilian program. In fact, U.S. intelligence believes that Iran is working on the technology to deliver a nuclear warhead on a missile; Secretary of State Colin Powell indicated he had seen "information that would suggest that they have been actively working on delivery systems....There is no

doubt in my mind...that they have been interested in a nuclear weapon".⁸⁰ Secondly, an indigenous Iranian nuclear program -- no matter the safeguards Tehran was prepared to accept and could as easily discard -- is unacceptable to Washington given the track record of covert nuclear activities and support for violent groups in the Middle East. And thirdly, while showing great enthusiasm for providing incentives to Iran, Europe will lack resolve if and when the time comes to impose sanctions. "The Europeans are fond of saying that they will stand with us if Iran breaches its commitments", a U.S. official remarked. "But when we ask them for specifics on the sanctions they would impose, all we get is a blank stare".⁸¹ There is even less faith in Russia or China, both of which have been investing heavily in Iran and would be loath to sacrifice their lucrative ties.⁸²

While the U.S. goal may be clear, means of achieving it are anything but. In fairness, the three principal options broadly available are far from promising: counter-proliferation, including a possible military strike; regime change; or pursuit of a comprehensive diplomatic deal.

A *counter-proliferation strategy* could include sanctions to slow down Iran's nuclear program and/or a pre-emptive military strike aimed at Iran's nuclear facilities. Sanctions could both heighten the cost of the nuclear program and, by targeting all technology potentially relevant to that program, hamper Tehran's efforts. In its most pronounced version, a sanctions regime would entail interdiction of land, air or sea cargo suspected of delivering nuclear technology. However, the U.S. trusts the international community neither to impose real sanctions, given general reluctance to go down this path and Iran's centrality to the oil market, nor, assuming it does impose them, to sustain them. As precedents show, moreover, Iran

⁷⁵ Crisis Group interview, Washington, October 2004.

⁷⁶ According to an EU official, "The U.S. is sitting on the sidelines, wishing the Europeans well, but taking no part in this. All the carrots on the table are from the Europeans; the U.S. has added nothing and not given the Europeans any authority to make commitments for it". Crisis Group interview, Brussels, October 2004.

⁷⁷ Crisis Group interview with European and U.S. diplomats, Washington, October 2004.

⁷⁸ Crisis Group interview with U.S. official, Washington, October 2004.

⁷⁹ Ibid.

⁸⁰ Quoted in the *The Washington Post*, 18 November 2004.

⁸¹ Crisis Group interview with U.S. official, Washington, November 2004.

⁸² The notion that Tehran's leaders are rational actors who would not take steps likely to endanger regime survival is of only modest comfort to U.S. officials: "Sure, the regime is rational, but its deep-seated hostility to the U.S. and insular view of the world lead it to an irrational 'connection of the dots'. For example, it sees our policy in Iraq and toward them as driven by a desire to suppress Shiites worldwide. It remains prone to take dangerous actions for what in its mind would be perfectly logical reasons, but that could set off a very dangerous and unplanned chain reaction". Crisis Group interview with U.S. official, Washington, November 2004.

would have considerable opportunity to thwart such measures.⁸³

Pre-emptive military action presents even greater risks for very uncertain pay-off.⁸⁴ A surgical strike aimed at disrupting the nuclear program would face considerable practical obstacles due to unreliable intelligence and the likely dispersal of nuclear facilities. Iran's retaliatory options are equally troubling, ranging from support for violent activity by armed groups and missile attacks against Israel, to steps to further destabilise Afghanistan and, especially, Iraq. (Hizbollah's unprecedented dispatch of a small drone over Israel on 7 November 2004 was widely interpreted in Lebanon as -- among other things -- an indirect message from Iran to both Israel and the U.S. that it had retaliatory capacity).⁸⁵ The likely effect also would be to strengthen the already emboldened hard-line faction in power, deal yet another blow to the reformists and alienate a population otherwise rather sympathetic to the U.S. -- in other words, making it more likely that if Iran acquires a full-fledged nuclear program it will be ruled by its potentially most worrisome faction. While this option has its advocates and will remain on the table, it is far from attractive.⁸⁶

Regime-change fomented from the outside is an objective seldom far beneath the surface. It appeals in particular to those who have given up on (or never had) the notion that the current regime's behaviour can be reformed in any significant way and believe that the best hope is to change the character of the regime before it acquires a nuclear arsenal. Given deep-seated structural problems and fissures in the

country (galloping demography; economic inefficiency; the gap between popular aspirations for change and repressive rule), there is confidence that sooner or later the regime will collapse. The U.S. priority, many argue, must be to accelerate this through a combination of covert action, sanctions, coercive diplomacy, support for dissident groups and avoidance of any initiative that might prolong the Islamic Republic's life-span.⁸⁷

While popular discontent remains deep and widespread, transcending age, socio-economic class, and geographic location,⁸⁸ the Iranian public has shown little signs of unrest since the summer 2003 student-led protests.⁸⁹ Nor do there appear to be indications of regime instability in the short term. "The main strength of the regime", a European diplomat told Crisis Group, "is the fact that at the moment there is no alternative".⁹⁰ Student groups remain inexperienced and disorganised, exiled opposition groups have insufficient popular support, and the vast majority of Iranians are far more focused on economic sustenance than on political deliverance. High oil prices also have provided the regime with an additional cushion. For reformists, the lesson is clear: years of U.S. pressure and containment have done little to modify the regime's behaviour, let alone bring about its downfall. Sanctions in particular are deemed to be highly counter-productive -- "the worst case scenario"⁹¹ -- likely to inflict far more damage on them than on the regime.

In other words, even with stepped-up U.S. efforts, significant political change seems highly unlikely in the short to medium term. In the meantime, the development of an offensive nuclear program

⁸³ The downsides of sanctions and an interdiction approach are further discussed in ICG Report, *Dealing with Iran's Nuclear Program*, op. cit., pp. 29-30.

⁸⁴ On this, see *ibid*, pp. 30-31.

⁸⁵ Crisis Group interviews with Lebanese analysts and foreign diplomats, Beirut, November 2004. The drone allegedly was supplied by Iran. Amid indications that Syria is moderating its policies in response to increased U.S. pressure, some Hizbollah leaders reportedly have been pushing for an even closer alliance with Tehran as insurance policy against a Syrian reversal. Crisis Group interviews, Beirut, November 2004.

⁸⁶ Advocates of a military strike accept that the relevant sites are dispersed and that some may not be known but suggest that if even half the capacity were taken out by precision munitions with earth penetrating capabilities, the Iranian program would likely be set back years. Some also suggest that if Iran were to retaliate by adopting an active policy of political and military sabotage in Iraq, it would expose its assets to identification and destruction. Crisis Group communication with former senior U.S. military official, November 2004.

⁸⁷ Crisis Group interview with U.S. official, Washington, October 2004.

⁸⁸ Aside from the overwhelming popular discontent in Tehran, unhappiness with the government is very much in evidence even in traditional towns and religious centres. According to one Qom shopkeeper, "If we had a democracy that represented the true spirit of the prophet Ali, it would be the best system. But our religion has been corrupted...the young generation doesn't believe in anything anymore". More Iranians have come to the same realisation as this former *basij* in Mashad: "In politics you are obliged to lie, but our religion forbids us to lie. It was a mistake to mix these two; it brings down the name of religion". Crisis Group interviews, Qom and Mashad, October-November 2004.

⁸⁹ For further discussion regarding Iranian popular discontent and student protests, see ICG Briefing, *Iran: Discontent and Disarray*, op. cit.

⁹⁰ Crisis Group interview, Tehran, October 2004

⁹¹ Crisis Group interview, Tehran, 4 November 2004.

would continue, without any incentive to slow it down. In the putative race between Iran's military nuclear program and regime change, there is every indication the former would prevail.

Whatever limited appetite for a full-scale military invasion existed prior to the Iraq war inevitably has been further reduced, despite President Bush's re-election. As a former U.S. official notes, "the Iranian population is nearly three times as large as that of Iraq, the country's geographic area is four times that of Iraq, and its terrain is awful", not to mention the violent resistance U.S. forces would face in the wake of an invasion.⁹²

A policy of broader engagement would start from the premise that neither of the two previous options is feasible. The administration -- divided on Iran policy to the point of "paralysis"⁹³ -- has not been prepared to adopt any form of sustained diplomatic engagement, aside from periodic, short-lived and issue-specific communications.⁹⁴ For the most part, its opposition is based on the conviction that Iran's ability to cheat far exceeds the ability of the IAEA or any other international body to verify and that rewarding Tehran with economic ties runs the risk of strengthening the regime, thereby further delaying the prospects of political change.

As a result, the U.S. has been unable to test whether a package of incentives and disincentives -- for example along the lines suggested by the EU -- might persuade Iran to drop its nuclear ambitions. Putting forward the prospect of a deal comprising U.S. guarantees on regime change and regional security together with promises of economic ties would make sense regardless of one's views on Iran's nuclear intentions. *Even assuming the most benign interpretation* -- that the nuclear program is a card Iran is ready to trade away -- it almost certainly will not turn it over in exchange for European guarantees when the party that represents both the greatest security and political threat and potentially

represents the greatest economic prize -- the U.S. -- is not even playing.⁹⁵

Conversely, *assuming Iran is determined to develop a military program*, the U.S. will not achieve international consensus unless it shows good faith willingness to deal. U.S. officials complain about the reluctance of others to apply sanctions. Iran's role as an oil exporter and its astute choice of economic partners certainly make this a hard sell. But a forward-leaning U.S. proposal is necessary to get the EU and other members of the international community to agree to a robust response in the event Iran turns it down. Setting forth the possibility of economic steps -- WTO accession and, gradually, normalisation of relations with the U.S. -- would have the further effect of exacerbating divisions among Iranian conservatives, strengthening those who favour closer integration in the world economy, and heightening the opportunity costs to Iran of violating its commitments. Conceivably, it could give some regime factions added reason to pause before developing a nuclear weapon or, at a minimum, moderate the character and the policies of the leadership that eventually possesses it.⁹⁶

Membership in the WTO and greater integration into the international economic system often are described as rewards for the Iranian regime. I think they are best seen as poison pills: sharpening divisions between those with an interest in more open trade and those who rely on domestic monopolies and increasing the costs to Iran of violating its international commitments.⁹⁷

Indeed, the current situation is a perfect illustration of the shortcomings of the present approach: without U.S. participation, the October 2003 agreement was bound to collapse; because the U.S. was not a party, the collapse was not -- nor could it rightfully be -- read as proof of Iran's intentions. In this respect, U.S. strategy -- as recently described by Deputy Secretary of State Richard Armitage -- has it exactly backwards: "My view", he stated, "would be that the incentives of the Europeans only work against the

⁹² Kenneth M. Pollack, *The Persian Puzzle* (New York, 2004), p. 382.

⁹³ Crisis Group interview with U.S. official, Washington, October 2004.

⁹⁴ See ICG Report, *Dealing with Iran's Nuclear Program*, op. cit., p. 22. According to Iranian sources, the administration purportedly rebuffed Iranian suggestions of a grand bargain suggested by Tehran in spring 2003, a time when Washington admittedly was consumed by the Iraq war. Crisis Group interviews, Washington, November 2004.

⁹⁵ This is widely acknowledged by EU officials. Crisis Group interviews with EU diplomats in Tehran, Washington and Brussels, October-November 2004. *The Economist* put it well: "the Americans are expecting co-operative behaviour from a regime whose neighbourhood they have occupied and whose legitimacy they do not accept", 4 September 2004.

⁹⁶ For a discussion, see Pollack, op. cit., pp. 378-379.

⁹⁷ Crisis Group interview with Iran analyst, Washington, November 2004.

backdrop of the United States being firm on this issue....It's kind of a good-cop, bad-cop arrangement".⁹⁸ Yet, without U.S. incentives, and in the absence of EU threats, prospects of a lasting deal are slim.

B. ISRAEL

While Washington clearly remains the most influential player, Israel would feel directly threatened by a nuclear-armed Iran and has suggested it might act to prevent it. Israeli security officials are convinced that Tehran is playing an active role, through Lebanese Hizbollah, in funding and orchestrating armed attacks in the West Bank; equipped with a nuclear bomb, they fear, it would present a considerable risk while becoming immune to outside pressure.⁹⁹ There is virtually wall-to-wall agreement across Israel's political spectrum that this is "a major tactical and strategic threat"¹⁰⁰ and that the international community has only a very small window in which to deal with it.¹⁰¹ For Major-General Aharon Zeevi-Farkash, head of the IDF's Military Intelligence (AMAN), "once they have the ability to produce enough enriched uranium, we estimate that the first bomb will be constructed within two years, i.e. the end of 2006 or the beginning of 2007".¹⁰²

Tensions have been on the rise, with officials from both sides raising the spectre of military confrontation. In August 2004, Baqer Zolqadr, commander of the IRGC, warned that Israel "would permanently forget about (its) Dimona nuclear centre, if it fires one missile at the Bushehr atomic power plant", evoking "terrifying consequences". Referring to its Shahab-3 missile, he added, "the entire Zionist territory...is now within range of Iran's advanced missiles".¹⁰³ Israeli

officials delivered their own warnings. In his 25 October 2004 Knesset speech, Prime Minister Sharon referred to "the most prominent danger", Iran, "which is making every effort to acquire nuclear weapons and ballistic missiles".

Like the U.S., however, Israel possesses few attractive alternatives. A repeat of the 1981 attack on Iraq's Osirak reactor¹⁰⁴ is considered possible, but hardly appealing. The great distances involved, the dispersal of facilities, and Iran's significant retaliatory options, all weigh in the balance.

There is no single tempting target like there was with the reactor at Osirak in 1981....Plus, if Israel were to attack, it would leave itself open to retaliation by Iran both regionally and worldwide through terror networks and Hizbollah, missiles.¹⁰⁵

As a result, while clamouring for tougher action and vocally sceptical about the EU deal (a high-ranking Israeli official noted, "we have the highest respect for Iran's ingenuity for hoodwinking the governments and NGOs of the world in order to achieve its strategic aims...Iran has no intention at all to change its policy"),¹⁰⁶ Israel so far has let diplomacy run its course. Indeed, U.S. officials told Crisis Group that their Israeli counterparts had discretely encouraged them to assess a variety of non-military options.¹⁰⁷ There also is the more unspoken concern that turning this issue into an Israeli-Iranian bilateral affair would increase the danger of putting Israel's own nuclear

considered "an attack on Iran as a whole, and we will retaliate with all our strength".

¹⁰⁴ See ICG Report, *Dealing with Iran's Nuclear Program*, op. cit., p. 30.

¹⁰⁵ Crisis Group interview with Aluf Benn, *Ha'aretz* diplomatic correspondent, 2 November 2004. The conservative Iranian columnist Amir Mohebbian made this explicit in an interview with Crisis Group: "Israel knows that if it attacks Iran, it will not receive the first missile from Iran, but from south Lebanon. According to different estimates there are 22,000 or 28,000 missiles in south Lebanon. They are directed at Tel Aviv. Israel has no strategic depth. So, Israel can fight very strongly with an army, but we see it is forced to withdraw from south Lebanon....Israelis are much wiser than Americans. They will not attack us". Crisis Group interview, Tehran, 23 September 2004.

¹⁰⁶ Crisis Group interview, Tel Aviv, 9 November 2004. Ephraim Sneh, another prominent Labour parliamentarian, charged that Iran was "toying with the EU". Crisis Group interview, 31 October 2004.

¹⁰⁷ Crisis Group interview with U.S. official, Washington, October 2004.

⁹⁸ Quoted in *The New York Times*, 21 November 2004.

⁹⁹ Crisis Group interview with Israeli diplomat, Washington, November 2004.

¹⁰⁰ Crisis Group interview with Israeli official, Tel Aviv, 9 November 2004.

¹⁰¹ Crisis Group interviews, Tel Aviv, October-November 2004. Haim Ramon, a prominent Labour member of the Knesset, made the case that Iran was "an immediate threat to Israel" -- indeed, its "only strategic threat" -- by underscoring that it is the "only state in the world that threatens to destroy a sovereign UN member state [Israel]". In his words, Iran's weapons currently are "the most important issue among decision-makers" in the defence/foreign policy establishment. Crisis Group interview, Tel Aviv, 4 November 2004.

¹⁰² Quoted in *Jane's Intelligence Review*, 19 August 2004.

¹⁰³ United Press International, 9 August 2004. Iran's Minister of Defence, Shamkhani, stated that a strike would be

arsenal on the table, something that "is totally non-negotiable in any way".¹⁰⁸

For now, the Israeli position is for the international community to hold Iran to very stringent conditions, including:

- immediate freezing and subsequent dismantling of any fuel cycle activities and facilities; the freeze needs to occur before Iran accumulates a strategic amount of uranium hexafluoride gas (UF6) and successfully operates its first cascade;
- at most, and as part of the agreement, Iran can be provided with a light water reactor and with a guaranteed supply of leased fuel which would have to be promptly returned to the supplier;
- such arrangements would have to be subject to intrusive verification, including the right to inspect non-nuclear manufacturing sites; and
- they would have to be anchored in a UNSC resolution.¹⁰⁹

But Israeli patience is almost certainly limited. Iran's ability to produce large quantities of highly enriched uranium is widely considered a red line, which, if crossed, could well invite forcible action.¹¹⁰ Ephraim Sneh, a Labour member of the Knesset and chairman of the Defence Planning and Policy Committee, remarked that Israel possesses four layers of defence -- passive (such as shelters); active (the Arrow missile system); responsive (missile interception); and preemptive (targets beyond Israel's immediate borders) -- and that it will not allow itself to wake up and "discover that we were irresponsible to allow these things to happen....One day we will act forcefully against Iran if no other solution is found".¹¹¹

¹⁰⁸ Crisis Group interview with Israeli official, Tel Aviv, 9 November 2004.

¹⁰⁹ Crisis Group interview with officials at Israel's atomic energy agency, Tel Aviv, November 2004.

¹¹⁰ Crisis Group interview, Tel Aviv, September 2004; see also Gerald Steinberg in the *Los Angeles Times*, 22 October 2004: "Nuclear weapons in a country with a fundamentalist regime, a government with which we have no diplomatic contact, a known sponsor of terrorist groups like Hizbollah and which wants to wipe Israel off the map -- that makes stable deterrence difficult, if not impossible".

¹¹¹ Crisis Group interview with Sneh, op. cit. Israeli analysts make clear that the preference is for U.S. action, considered logistically far easier and politically less risky. Crisis Group interview, Tel Aviv, 9 November 2004.

V. WHERE NEXT?

While IAEA Director General ElBaradei has continued -- apparently accurately -- to state that there is no hard evidence of an Iranian military nuclear program, the circumstantial evidence is assuming increasingly damning proportions. The IAEA has noted that Iran has repeatedly violated its commitments under the NPT Safeguards Agreement, and that its dealings with the Agency frequently lack transparency. U.S. intelligence sources continue to assert that Iran is pursuing a military program, noting most recently intensified efforts at uranium conversion and at building a missile capable of carrying a nuclear payload. And the Iranian exiled group that first helped expose Iran's concealed activities in 2002 claimed that Iran was still enriching uranium at a secret location and had received blueprints from Pakistani scientist A.Q. Khan.¹¹²

Of course, there is reason to be sceptical about these claims. The reliability of U.S. intelligence has been badly tainted by the Iraqi debacle, and the Iranian opposition group -- the National Council for Resistance in Iran (NCRI) -- has every reason to try to discredit Tehran, particularly in the wake of the EU deal and on the eve of the IAEA meeting. While some of its information has proved accurate, much else has not, and it has had a marked tendency to make inflammatory allegations with a transparent agenda of promoting regime change.¹¹³

Still, the safer bet for now is to assume that Iran is developing the capacity to build a bomb, the question being whether it already has made a strategic decision to go forward or whether it is a card it might be prepared to barter under appropriate conditions.¹¹⁴ Under either scenario, the current approach is fated to fail. At this point:

¹¹² Elaine Sciolino, "Exiles add to claims on Iran nuclear arms", *The New Times*, 18 November 2004.

¹¹³ As observers have noted, "Iraqi dissident claims about Saddam Hussein's weapons were equally detailed and specific, but none proved to be true". Revati Prasad and Joseph Cirincione, "New Allegations Against Iran", Carnegie Endowment, 18 November 2004.

¹¹⁴ "It appears likely that Tehran does not have a determined nuclear-weapon program, such as Iraq had in the 1980s ... but that it intends to acquire the capabilities to produce nuclear weapons should the government decide to do so in the future". Miriam Rajkumar and Joseph Cirincione, "The IAEA's Report

None of the parties has put its true cards on the table. Iran has yet to indicate its bottom line: whether it wants a nuclear capacity or the dividends and bargaining power such dividends would yield. The U.S. has been paralysed and unwilling to engage. As for the EU, it has sought to pick up the pieces but without the necessary carrots and sticks.¹¹⁵

What is needed to change this picture is enhanced U.S./EU coordination and a joint serious offer with U.S. participation.

A. THE CONTOURS OF A DEAL

1. Iranian compliance with the November 2004 agreement:

In the short run, the new agreement offers far more specificity as to what Iran needs to do -- continue to abide by the terms of the Additional Protocol, allow unfettered inspections, and most importantly suspend all uranium enrichment activities as defined.

2. Negotiations over a long-term agreement:

As soon as Iran's compliance has been verified, negotiations need to get underway on a longer-term deal.

Iran. As described in Crisis Group's previous report, basic elements should include steps to satisfy the U.S., EU and others that it does not intend to develop a military program. Ideally, this would include renunciation of its right to an indigenous yellowcake-to-enrichment capacity and, therefore, dismantling of its existing facilities in exchange for a guaranteed supply of fresh reactor fuel coupled with retrieval and storage of spent fuel by the supplier. But Tehran is unlikely to acquiesce¹¹⁶ (at least in the context of the current climate of hostility toward and mistrust of the U.S., perhaps ever) and -- short of a generalised modification of the NPT -- neither are a number of significant international players. As a

fallback, Iran should be asked to agree to joint Iranian/international management of the sites, a type of condominium arrangement in which the UK, for example, would play a lead role.¹¹⁷

The U.S. and EU. The list of benefits desired by Iran is relatively well known: the provision of advanced civilian nuclear technology, conclusion of a preferential trade agreement with the EU, security guarantees based on the principle of non-interference in internal affairs and respect for sovereign states, and recognition of Iran's regional security interests, eventually under the aegis of a regional forum. Key to this process will be U.S. readiness not only to support EU actions but to take some of its own. The U.S., the EU and other relevant players -- including notably Russia, China and Japan -- will need to lay out up front what benefits Tehran would receive if it were to agree to restrictions on its nuclear program that go beyond the NPT and Additional Protocol. This could comprise security assurances (dealing with both regime change and the regional situation, including the establishment of a regional security forum), trade and investment, the provision of civil nuclear technology, support for WTO admission, and a pragmatic path to normalisation of relations with the U.S.¹¹⁸

3. Options in the event of a breakdown:

Should Iran either renege on its November 2004 commitments or, in the face of a subsequent serious and good faith offer, fail to agree, sanctions will need to be applied. Ideally, these would be authorised by a UNSC resolution; failing that, they should be imposed by a large coalition of like-minded countries, including G7 partners and, if possible, Russia and China. To persuade the U.S. to present its incentives, these countries should commit up front to supporting a menu of pre-determined sanctions should they become necessary. Even if Iran has already mastered the entire fuel cycle, it would face many practical engineering problems were it to seek to move to large-scale production of highly-enriched uranium and nuclear weapons, and these difficulties would be enhanced if

on Iran: No Slam Dunk", Carnegie Endowment, September 2004.

¹¹⁵ Crisis Group interview with U.S. official, Washington, October 2004.

¹¹⁶ Moussavian, a top Iranian negotiator, asserted: "The Islamic Republic cannot rely on the fuel the Europeans are offering, because they might withdraw it any time there are differences in relations. We need to become independent in providing our own fuel". Quoted in *The New York Times*, 25 October 2004.

¹¹⁷ EU diplomats have indicated an open mind to such a model. Crisis Group interviews, Paris, Tehran, October-November 2004.

¹¹⁸ Listing what Iran expected from the U.S., Dr. Mostafa Zahrani, an official at the Foreign Ministry, mentioned acceptance of Iran as a regional power, an end to sanctions and a halt of all talk of regime change. Crisis Group interview, Tehran, September 2004.

sanctions were imposed. Multilateral sanctions could be imposed on an incremental basis, and include:

- ❑ a ban on the sale or transfer of all nuclear and missile technology and dual-use technology;
- ❑ a ban on the transfer of conventional weapons;
- ❑ a moratorium on new economic agreements with Iran;
- ❑ a ban on all new investment in Iran's gas industry;
- ❑ restrictions on non-oil or gas imports from Iran;
- ❑ a ban on new contracts for the import of Iranian gas;¹¹⁹ and
- ❑ imposition of land, air and sea interdiction regimes to prevent Iranian import of nuclear or dual use technologies.

Nonetheless, while sanctions might become necessary, there is little doubt that they are only moderately appealing. At this point, they would constitute punishment far more than prevention; assuming Iran is determined to develop a bomb, it will be extremely difficult to stop it. Nor, as seen, is it likely that sanctions would destabilise the regime, which has demonstrated a remarkable ability to withstand popular discontent and which likely would use international isolation as a means of tightening its hold and rallying support.¹²⁰

The optimal solution clearly is diplomatic and ought to be given a serious try. Given the dearth of satisfactory alternatives, failure of this path likely would mean having to learn to live with a nuclear Iran.

Amman/Brussels, 24 November 2004

¹¹⁹ Sanctions targeting the oil sector could have a crippling economic effect but most experts believe them to be unlikely given international dependence on Iranian oil and the impact they would have on already high oil prices. Moreover, Iran's easy access to international waters, its porous borders and its readiness to commercialise its lucrative oil and gas sectors would undermine the effectiveness of sanctions, should they be imposed.

¹²⁰ The President's brother, Mohammadreza Khatami, warned that sanctions would only undermine the development of democracy in Iran. Crisis Group interview, Tehran, November 2004.

APPENDIX A
 MAP OF IRAN





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