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Iran and Pakistan Gas Pipeline – Options for Pakistan

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Executive Summary

Iran – Pakistan gas pipeline can be subject to US sanctions. This brief attempts to explore the most effective ways to counter these sanctions. It explores different mechanisms to counter the impact of these sanctions which include *inter alia* financial, legal, and political mechanisms. It also attempts to divulge the experiences of different nations such as Russia in countering US Sanctions. In addition to outlining different hindrances to the Iran – Pakistan gas pipeline, the brief also establishes the necessity in terms of gas requirements of Pakistan which highlights the importance of the Iran – Pakistan gas pipeline. Lastly, the brief reiterates the huge repercussions for Pakistan in not complying with both US sanctions and the Iran – Pakistan gas pipeline agreement to stress the government in finding innovative solutions to counter this complex position.

Following are the brief recommendations: -

- Pakistan must lobby in the US for a waiver. In these negotiations, it must be stressed that these sanctions violate the basic premises of international law. This shall be an important element of advocacy even if there is no concern for Americans.
- The best way shall be to negotiate with Iran a mechanism for the payment of Iranian gas in a currency other than US dollars. It can be either through accepting the currency of Pakistan or clearing the transactions in the Chinese Yuan.
- Pakistan can also create a special-purpose vehicle that clears all financial transactions through the barter system or under a joint currency swap.
- Pakistan shall have to adopt legislation and create legal teams that provide legal support and assist those entities that are under the radar of US sanctions.
- Pakistan shall have to adopt a blocking statute that prevents entities in Pakistan from complying unnecessarily with US sanctions.

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Introduction

In 2009, Pakistan and Iran signed a Gas Sales Purchase Agreement ('GSPA') under which Pakistan was to import 750 mmcf of gas from Iran.¹ Iran claims that it has completed the construction of 900 km of pipeline in Iranian territory while Pakistan has not even started construction. Iran now repeatedly threatens Pakistan with a case in international arbitration which can result in a penalty of around \$18 billion. Therefore, the caretaker government of Pakistan accorded approval to the project with the initial construction of 80 kilometers of pipeline.² This pipeline portion is in Pakistani territory so there is no threat of sanctions from the United States ('US'). However, for the complete functioning of the project in the future, Pakistan shall request a waiver from the US about conducting economic relations with Iran for this pipeline project.³

Major Hindrance

It is unlikely that the US shall be taking sanctions off from Iran as the US has continued to impose sanctions on Iran since 1979 and their firms do not have much market share in Iran. The major hindrance in the execution of the IP Gas project is the US sanctions on Iran as the US claims that Iran is supporting terrorism and is complicit in human rights violations. The US is adamant that it will not grant further exemptions to importers of Iranian oil and petroleum products.⁴ It is also unlikely that these sanctions shall be removed soon as the US does not desire to remove leverage associated with sanctions while Iran also has no trust for the US for any peace deal as the Presidential powers to invoke sanctions can make the process in a very swift manner against Iran.⁵ Congress also has a considerable role in reviewing the statutes governing removal from the terrorism list which makes the process cumbersome as the US government needs to prove to Congress that there is a fundamental shift in the policies of the Iranian government.⁶

¹ Khalid Mustafa, 'Pakistan – Iran to sign extension in IP gas line agreement next week', *The News*, September 1, 2019

² Sarah Zaman, 'No Need for US Waiver to build Gas Pipeline with Iran', VOA, March 21, 2024

³ News Desk, 'Pakistan to Seek US Waiver for Iran Gas Pipeline Project', Tribune, March 25, 2024

⁴ Elizabeth Rosenberg, "Assessing the Use of US Sanctions in Addressing National Security and Foreign Policy Challenges", Center for a New American Security (2019), pp 5.

⁵ Richard N. Haas, 'From Sanctions to the Soleimani Strike to Escalation: Evaluating the Administration's Iran Policy' Council on Foreign Relations (2020)

⁶ Kenneth Katzman, 'An Analytic Compendium of U.S. Policies, Laws, and Regulations' Atlantic Council (2011),169

Iranian Sanctions Act also requires the US government to show that Iran has ceased efforts to develop nuclear weapons and that Iran no longer is a threat to US interests.⁷ These sanctions allow the US to impose sanctions extraterritorially on firms and multinational corporations that attempt to evade US sanctions.⁸

Necessity of the Project

It is argued that this project is economically beneficial for both countries. Pakistan does require Iranian gas for energy security as natural gas accounts for a major portion of the energy mix of the country. Pakistani gas reserves are depleting, and the country is increasingly relying on Liquefied Natural Gas to accommodate the import requirements with requirements reaching 1,900 million cubic feet per day (MMCFD) by 2030.⁹ Only 25% to 27% of the citizens have access to gas in Pakistan.¹⁰

Violation of International Laws

Under international law, unilateral sanctions violate the Charter of the United Nations and the authoritative 1970 Declaration of Friendly Relations and Cooperation among States. These sanctions violate the basic principles of international law which include juridical equality of States; the principle of self-determination of people and the principle of non-intervention. United Nations Sanctions, adopted under Chapter VII of the United Nations Charter, are the only sanctions that have international law validity.¹¹ Retorsions are also arguably only legal when they are not used to coerce a state ‘to concede a matter within its *domaine reserve*’.¹² It must be noted that UN sanctions do not bar Iran from energy cooperation with the outside world as it only aims to pursue the nuclear capability of Iran.¹³

Waiver from the US

The legal way to evade sanctions is to request a waiver from sanctions. Under Section 9411 of the US Code, the President of the United States has the power to issue a waiver for 180 days

⁷ Ibid, 171

⁸ Journal of Political Studies, University of the Punjab (Vol. 20, Issue-2, Winter – 2013).

⁹ Planning Commission, Pakistan Energy outlook Report (2021 – 2030), pp 3

¹⁰ Ibid (n.3)

¹¹ Asian-African Legal Consultative Organization (AALCO), ‘Unilateral and Secondary Sanctions: An International Law Perspective’, *Secretariat Study*

¹² Marco Milanovic, ‘Revisiting Coercion as an Element of Prohibited Intervention in International Law’, *American Journal of International Law*, Volume 117, Issue 4, October 2023, pp. 601 - 650

¹³ Ibid (n.9)

and renew it for another 180 days.¹⁴ However, the trend in Washington is that such waivers are not appreciated anymore. In 2019, President Trump revoked significant exemptions from eight countries including China and India.¹⁵ To acquire a waiver, support from certain countries such as Saudi Arabia and the United Arab Emirates (UAE) shall be essential and the waiver shall require intense negotiations with US.¹⁶

Ways to Avoid US Sanctions

The American power to enforce their sanctions stems from their ability to control the global financial system. The Society for Worldwide Interbank Financial Telecommunication ('SWIFT') dominates the financial transactions network which is under the control of the US. As most financial transactions are denominated in dollars, the place of clearing transactions remains in New York. Therefore, to evade US Sanctions, the only way is to transact less in US Dollars. Both the European Union and China realize this issue and are aiming to create their own version of financial telecommunications.¹⁷ China has created a Cross-Border Interbank Payment System ('CIPS') which settles financial transactions in the Chinese Yuan.¹⁸

Another way in which countries are aiming to evade US sanctions is creating a barter system of trade. For trading with Iran, a special-purpose vehicle can be created that allows only the exchange of goods rather than money changing hands. This shall enable a total absence of any reliance on US Dollars.¹⁹ EU has also specifically created blocking statutes for EU persons to comply with US sanctions. This is designed to ensure that there is no impact on the rulings of foreign courts in the EU which are premised based on US sanctions.²⁰

Russia was able to reduce reliance on US dollars by creating a network of subsidiary companies with no clear resemblance to each other. In a way, creating a giant *Matryoshka* doll i.e., dolls of decreasing size placed one inside another. In this model, sanctioned goods like chips were able to reach Russia.²¹ Another route adopted by Russia was to use a third country for importing goods. For instance, Kazakhstan sold 3.3 million Euros worth of semiconductors

¹⁴ 22 USC 9411: Presidential waiver authority

¹⁵ Cortney Morgan, Grant Leach, Katherine Stubblefield, 'President Trump to End Sanctions Waivers for Iranian Oil' *International Trade Insights* April 26, 2019

¹⁶ Zofeen T. Ebrahim, 'Analysis – To build or not to build - the Iran Pipeline Conundrum' *DAWN* April 20th, 2024

¹⁷ News Desk, 'Can the EU bypass US sanctions on Iran?' *TRT World*, 2019

¹⁸ News Desk, 'Unlike Russia, China can bypass SWIFT to escape the ambit of US power' *Bloomberg* 28th Feb 2022

¹⁹ *Ibid* (n.17)

²⁰ *Ibid*

²¹ Anna Romandash, 'How to get away with sanctions, Russian-style' *IPS – Journal* 16th March 2023

to Russia.²² China is also a popular and strong country with enough leverage for Russia to procure goods.²³

To protect itself from US sanctions, Iran has created legal services to assist internationally and domestically those people who are at risk of US sanctions due to trading with Iran. Iran has also attempted to provide mismatched certificates of origin from non–Iranian businesses to evade sanctions.²⁴

Repercussions for Evading

In case, Pakistan can successfully reduce reliance on US Dollars, Pakistan still can be culpable of violating US Sanctions. As a result, access to US markets might be constrained for the country. US Sanctions can be applied even if there is no direct contact with the US financial system. It can apply to any ‘U.S.- incorporated entity or foreign entities with U.S’.²⁵ It can also proscribe entities that engage with entities that the US deems as sanctioned. Non–Americans can opt between either engaging with the American market or with the sanctioned entity. For instance, SWIFT was given an ultimatum that they could either engage with the USA or Iran.²⁶ It is no surprise that Congress is moving forward to ‘pass new legislation to require the collection and disclosure of beneficial ownership information in the corporate formation processes.’²⁷ Unlike Iran, Pakistan drives foreign policy intending to preserve the balance between major powers.²⁸ If Pakistan constructs a gas pipeline with Iran, there is a probable chance that it shall signal to the West that Pakistan is moving closer towards Asian blocs.

Recommendations

Pakistan shall have to adopt a four-phase approach to proceed with GSPA:

- Pakistan must lobby in the US and UN forums for a waiver. In these negotiations, it must be highlighted that Pakistan is in a debt crisis already and any penalty shall be disastrous for Pakistan. For these purposes, Pakistan must insist that it is in the interests of the US that Pakistan is not forced completely to have no option but to exit from the

²² Navin A. Bapat and Bo Ram Kwon, When Are Sanctions Effective? A Bargaining and Enforcement Framework, International Organization, Winter 2015, Vol. 69, No. 1 (Winter 2015), pp. 131-162

²³ Anna Romandash, ‘Russia’s Handbook for Evading Sanctions’ Instick, July 11, 2023

²⁴ Newsroom, ‘Hacked Documents Reveal Iran’s Strategies to Bypass Sanctions’, *Iran International*, 13th February 2024

²⁵ Ethan Kessler, How Economic Sanctions are Used in U.S. Foreign Policy, Chicago Council on Global Affairs (2022)

²⁶ Ibid,

²⁷ Elizabeth Rosenberg, ‘Assessing the Use of Sanctions in Addressing National Security and Foreign Policy Challenges’ Center for a New American Security (2019)

²⁸ Dr. Aneel Salman, ‘Iran’s Incursion into Pakistani Skies; Economic and Defense Ripple Effects’ *Stratheia* January 18th, 2024

ambit of engaging reasonably with the USA based on mutual interest. In these negotiations, it must be stressed that these sanctions violate the basic premises of international law.

- Regardless of the decision of the US, Pakistan needs to slowly shift from reliance on US dollars. Pakistan has already negotiated an amendment in the GSPA for revising the timelines for the project.²⁹ Therefore, the best way shall be to clear payments under the Pakistan – Iran currency swap agreement, and Pakistani banks can also open their branches in Iran.³⁰ For that purpose, even an amendment under GSPA can be negotiated with Iran to create a specific provision for clearing payments under a currency swap agreement.
- For trading with Iran, Pakistan can also create a special-purpose vehicle that clears the majority of the financial transactions through the barter system. This shall require Pakistan to exponentially increase exports in those sectors that Iran requires on an urgent basis and at a cheap price.
- Despite finding ways to evade reliance on US dollars, there is a possibility that Pakistan comes under the ambit of secondary sanctions of the US simply for trading with Iran. For this purpose, Pakistan shall have to adopt legislation and create legal teams that provide legal support and assist those entities under the radar of US sanctions. Pakistan shall also have to adopt a blocking statute that prevents entities in Pakistan from complying unnecessarily with US sanctions.

²⁹ Newsroom, 'Amendment in Gas Sale Purchase Agreement with Iran being negotiated: Ministry' *APP* 8TH August 2016

³⁰ Editorial, 'Currency swap agreement with Pakistan on horizon: Iranian Ambassador' (*The Profit*, May 3, 2018)

Recommendations and Action Matrix

Legal Options for Government

Recommendations	Pathways to Solution	Implementation of Solution	Actors Responsible	Implementation Timelines
Waiver	Pakistan needs to narrowly tailor a request to the USA for a waiver in terms of the IP Gas pipeline. For this purpose, US Lawyers and lobbyists might have to engage.	Pakistan needs to stress the international law obligations of the US, the energy security of Pakistan, and the economic situation of Pakistan in these negotiations for a waiver.	<ol style="list-style-type: none"> 1. Ministry of Foreign Affairs 2. Ministry of Law 3. Ministry of Commerce 4. Attorney General for Pakistan 	1-2 Months for the request
Alternative Mechanisms	Pakistan shall have to negotiate with Iran either payment mechanism through barter trade or a third-party currency like Chinese currency	Amendment in GSPA in terms of payment mechanisms for clearing transactions through CIPS in China or a creation of a legal entity exclusively for barter trade.	<ol style="list-style-type: none"> 1. Ministry of Foreign Affairs 2. Ministry of Law 3. Ministry of Commerce 4. Ministry of Finance 5. Attorney General for Pakistan 	3 - 6 Months to formulate the Amendments.
Legislative Measures	To prevent any secondary sanctions, Pakistan shall have to create laws to block Pakistani companies from complying with sanctions and to protect any companies that interact with Pakistan.	Pakistan shall have to engage international law firms and create a specialized legal unit within the country to provide constant legal protections for the companies interacting with Pakistan. Moreover, the blocking statute shall also create a clear legal position for companies in Pakistan.	<ol style="list-style-type: none"> 1. Ministry of Foreign Affairs 2. Ministry of Law 3. Ministry of Commerce 4. Ministry of Finance 5. Attorney General for Pakistan 	3 -6 Months tentatively for the approval of legal amendment in the Act.

