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States Divest From Businesses Tied to Iran

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Eleven U.S. states have adopted legislation to divest public pension funds from companies with financial ties to Iran's petroleum, defense, and nuclear sectors in an attempt to persuade Iran to give up its uranium-enrichment program and alleged sponsorship of terrorism. Almost 20 more states are considering similar legislation to supplement existing federal and international sanctions.

This is the first time that state investments have been leveraged for nonproliferation goals. During the 1980s, anti-apartheid activists urged state and local authorities and some universities to divest holdings from companies invested in or doing business with South Africa. During the 1990s, humanitarian activists persuaded Massachusetts to divest from companies "doing business with" Burma (Myanmar). More recently, almost 30 states passed legislation to divest from companies with investments in or engaged in trade with Sudan. The Iran case is unique, however, because divestment legislation explicitly references Iran's alleged sponsorship of terrorists and its uranium-enrichment program.

Since the 2003 discovery of Iran's clandestine uranium-enrichment program, the UN Security Council has imposed three rounds of sanctions freezing the finances and limiting the travel of prominent members of the nuclear and ballistic missile programs (see page 39). Enriched uranium can fuel nuclear reactors and provide the explosive core for a nuclear weapon.

The effort by U.S. states to divest from Iran mirrors a larger change in the Bush administration's approach to Iran. For its part, the U.S. government has maintained various sanctions on Iran since 1979. Recently, however, Washington has moved away from advocating sanctions against individuals and organizations and toward a strategy of financial isolation. The Department of the Treasury in 2007 barred Iran's Bank Saderat, Bank Sepah, and Bank Melli from the U.S. financial system and cut off their ability to conduct transactions with U.S. banks through a third party. (See *ACT*, March 2007.) In March, the UN Security Council urged member states to "exercise vigilance" about the activities of these banks. (See *ACT*, April 2008.) Treasury officials have recently discussed sanctioning Iran's central bank, which is said to have picked up some of the business that used to flow to sanctioned institutions.

Legal Challenges

State divestment efforts also face legal challenges. The National Foreign Trade Council (NFTC) in 2000 successfully sued Massachusetts over legislation to divest from Myanmar. In that case, NFTC v. Crosby, the U.S. Supreme Court ruled that Massachusetts' decision hindered the president's ability to conduct foreign policy effectively. The NFTC won another legal battle in a U.S. district court over an Illinois law mandating divestment from Sudan.

Lawmakers have taken steps to circumvent subsequent court challenges. Several bills pending at the federal level encourage and authorize state divestments. The Iran Sanctions Enabling Act, introduced by Barack Obama (D-Ill.), the presumed Democratic presidential nominee, and Sam Brownback (R-Kan.) in the Senate and a bipartisan group of eight representatives in the House, would publish in the Federal Register the names of companies with $20 million or more invested in Iran's energy sector and authorize individual states to adopt divestment legislation.

The bill also provides legal safe harbor for fund administrators who might oppose divestment on grounds that doing so would cause their funds to depreciate. To this end, the bill protects mutual fund managers from lawsuits and pension

fund managers from charges of fiduciary responsibility. According to Missouri's treasurer, the Missouri portfolio suffered minimal disruption following divestment and in some years outperformed the original fund.

Divesting From Terrorism

Most divestment legislation adopts the criteria laid out in the 1996 Iran Sanctions Act to identify significant investment in Iran. Formerly the Iran-Libya Sanctions Act, it requires the president to sanction those foreign companies with investments of $20 million or more in Iran's energy sector.

In that vein, legislation signed in Arizona, California, Colorado, Florida, Georgia, Illinois, Louisiana, Maryland, and Michigan directs state pension administrators to divest from companies that meet this standard and companies with financial ties to Iranian "terrorist organizations" identified by the U.S. government. Also anathema are companies that facilitate Iran's acquisition of nuclear, chemical, or biological weapons technology or military equipment.

Missouri and New Jersey have adopted explicitly "terror-free" investment policies. Terror-free investing, part of a larger initiative endorsed by the American Israel Public Affairs Committee (AIPAC), the Center for Security Policy, and a number of other groups, encourages U.S. states to divest from companies "reasonably known to be operating directly with the government or a government-controlled agency in U.S.-sanctioned nations, or that are engaged in the sponsorship of terrorism." Known as the Divest Terror movement, proponents argue that investing in such blacklisted countries as Cuba, Iran, North Korea, Sudan, and Syria poses not just a threat to national security, but to the health of the investments themselves.

Of these countries, Iran stands the most to lose from widespread divestment from its economy. Iran's gross domestic product is greater than that of Cuba, North Korea, Sudan, and Syria combined—around $600 billion, according to most sources.

The movement has gained several prominent adherents, including presumptive Republican presidential nominee Sen. John McCain (Ariz.). In a June 2 speech at AIPAC's national convention, McCain called for a "worldwide divestment campaign" in order to pressure Iran's "radical elite."

The target of state divestments, both in practice and as a part of a broader strategy to pressure Iran financially, is to hurt companies with significant ties to Iran's energy sector. Companies potentially affected by divestments include such European giants as Spain's Repsol, France's Alcatel and Total, and Royal Dutch Shell. Some states' pension funds are too small to conceivably have an impact. On the other hand, California's Public Employees and State Teachers Retirement Systems invest a combined $400 billion in U.S. and international companies. An estimated $2 billion of those funds are tied up in Iran's oil sector.

Matthew Levitt, a former Treasury Department official in the Office of Terrorism and Financial Intelligence and director of the Stein Counterterrorism Center at the Washington Institute for Near East Policy, concedes that divestment alone will probably not force Iran to adhere to international demands. "The real issue is not divestment [by itself]," he says, "but the totality of the various [coercive] measures. Together they have a very good chance of forcing Iran to rethink its policies."

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