"The Iranian Situation"

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by

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It was with pleasure that I accepted the invitation to speak before the Section of Mineral Law. Although I am no longer engaged in the practice of the law, I still like to identify myself with members of the profession. Even though I have given up practicing law, I still continue to have problems and right now the Middle East, particularly Iran, presents all the problems any lawyer could seek. These issues concern important legal principles, but mixed with unusually strong doses of politics, personalities and business complications.

When I was asked to talk about the problems growing out of the so-called nationalization of the oil industry in Iran, I had hoped, perhaps without much conviction, that some reasonable settlement might have been agreed upon by now. Unfortunately this is not the case. The forces which have created this problem are dangerous. They are making it difficult to find solutions. Before the issues are settled, they are likely to engender further problems, both in Iran and in neighboring countries.

The situation in the Middle East is serious and is of primary importance in the many difficult problems facing us in the world. But unless we understand the issues involved, important principles may unwittingly be compromised in our extreme efforts to solve the troubles of any particular moment. A
violation of these principles could, in my opinion, seriously injure our interests elsewhere in the world and perhaps render meaningless in a relatively short time those expedient solutions for the Iranian problem.

To better understand what I have in mind, let us look at the historical facts concerning the Iranian oil concession. In Iran, as in many other countries outside the United States, the underground minerals are owned by the Government. This is an important fact to keep in mind and one to which I will revert later in this talk. In Iran, rights to search for oil and, if oil is found, to develop the oil resources must, therefore, be obtained from the Government and not from private individuals.

Such a contract was made in 1901 between the Government of Iran and what has now become the Anglo-Iranian Oil Company. Under this contract, Anglo-Iranian was given the right to search for oil in specifically defined areas in Iran and, if oil were found, to develop, transport and dispose of it in the world markets. In return the Iranian Government was to receive certain payments of money, and if oil were found it was to receive a specified royalty. The arrangement was to run until 1961, a period of sixty years. There were, of course, many other details covered by the contract, but it generally followed the pattern of oil agreements in that part of the world at the time it was made.

Based on faith in this contract, the Company invested substantial sums of money in Iran and oil was found in 1908.

(After)
After oil was found additional capital was attracted by the Company and Iran's oil was developed. By 1932 large sums of capital had been invested in Iran and production had reached 135,000 barrels daily. Relations between the Government and the Company were not always smooth and late in 1932 the Iranian Government announced the cancellation of the concession under which the Company was then operating. At that time the British Government made a vigorous protest against Iran's action.

After some sparring, Britain requested the League of Nations Council to consider the dispute between the oil company and Iran on the ground that it was a "dispute likely to lead to a rupture" pursuant to Article 15 of the League of Nations Covenant. The British Government had intended to initiate proceedings before the Permanent Court of International Justice, but when it became apparent that Iran would go to the League Council, thereby automatically staying the proceedings before the World Court, Britain went directly to the Council. Iran took the position at that time that the World Court had no jurisdiction over its cancellation of the concession on the theory that the dispute was not one subject to International Law, but simply a matter governed by Iranian law. Iran's position was never decided for, after a hearing before the members of the League of Nations Council in Geneva, the dispute was amicably settled by bilateral negotiations which resulted in a new concession agreement.

The new agreement was to last for a term of sixty years, until 1993. It was duly signed by the Imperial Government of Iran following its ratifications by the Iranian Parliament and had the (royal)
royal assent of the Shah. The 1933 agreement was freely entered into by the Iranian Government and gave to that country advantages of much greater value than those existing in the former concession agreement. Not only was the rate of royalty increased for the future, but that increased rate was paid retroactively for the years 1931 and 1932.

Article 21 of the new agreement provided:

"This concession shall not be annulled by the Government and the terms therein contained shall not be altered, either by general or special legislation in the future, or by administrative measures, or any other acts whatever of the executive authorities."

Thus the original agreement was modified by bilateral negotiations and under the modified contract the Iranian Government entered into a concession agreement with a foreign corporation which was a citizen of a nation whose relations were friendly with Iran. Further, the Iranian Government specifically agreed by Article 21 that it would take no official action either by the executive or legislative departments of the Government to cause the concession to be altered or cancelled for a period of sixty years.

Operating under this agreement, the Anglo-Iranian Oil Company constructed its huge refinery facilities at Abadan, an investment of several hundreds of millions of dollars. The Company discovered additional sources of oil and was producing at the close of 1948 a daily average of 550,000 barrels of crude. That output had been speeded up to 700,000 barrels per day at the time of (the Nationalization)
the Nationalization vote last March. However, during the latter part of this period the Government became dissatisfied and in 1946 it so notified the Company. In 1949, after three years of negotiations between the Anglo-Iranian Oil Company and the Iranian Government, the Company drew up a supplementary agreement to its 1953 concession based on these negotiations. Retroactive to January, 1948 it increased royalty payments by approximately 50 percent, permitted an additional flat tax of 1/- per ton and gave Iran an immediate 20 percent share in funds transferred to Anglo-Iranian's general reserves. Measured in the light of terms generally prevailing in the Middle East at the time, this proposed modification of the contract was generous to the Government.

In the summer of 1948, the Iranian Government's Executive Department, headed by the late Premier Ali Razmara, signed the agreement and it went to the Majlis, or lower house of Parliament, for approval. The Majlis failed to act in the short period before adjournment and the agreement was tabled. Placed before the new Majlis in June, 1950 the proposal was handed to a Commission of Deputies, headed by the present Iranian Premier, Mohammed Mossadegh, for study. These negotiations were being carried on at a time when there was a wave of extreme nationalism sweeping most of the Middle East countries. World politics were highly disturbed. In addition the entire political atmosphere of the Middle East had been inflamed by the Palestine question. These conditions made it very difficult to view any problem from a correct perspective.)
perspective. While the Commission studied, the extremists were busy agitating for what they called nationalization of the oil industry. Their main objective was to exclude any foreign elements from Iran. The term "nationalization" was not understood and became a symbol for this feeling of nationalism. Within a few months, on March 7th of this year, former Premier Razmara was assassinated. A week later the Majlis passed preliminary legislation to nationalize the oil industry and the Iranian Senate concurred. Razmara's successor, Hussein Ala, who had signed the 1933 agreement, held office only briefly. Ala resigned in protesting Parliament's approval late in April of the Iranian Oil Nationalization Act. Mossadegh, sponsor of the act, became premier.

When Iran broke its contract with Anglo-Iranian Oil Company by purporting to nationalize the Iranian oil industry, many thought - and apparently still think - that it only served the British right. For what can be more entertaining than the spectacle of one government nationalizing the property and rights of a company incorporated under the laws of another government which was in the process of doing a good deal of nationalizing of its own private industry? It was even more obviously sauce for the gander since the British Government itself owns a majority of the Anglo-Iranian Oil Company's stock.

But we must stop and soberly examine the issues involved. It is not merely a dispute between Iran and Britain which we can watch with amusement. It is a question of whether the spoken or
written word can be relied upon. Unfortunately there has been a
good deal of misunderstanding of what has actually happened. The
word "nationalization" has been accepted by too many people with­
out stopping to examine the facts.

The term "nationalization" means to establish national owner­
ship and control. It describes a process where a government
acquires possession and asserts title to property within its
borders which was formerly owned by private individuals.

The issue involving the Anglo-Iranian Oil Company in Iran
today is not accurately described as one of nationalization. In
point of fact the Iranian Government has always owned the oil
reserves. The concession it made with Anglo-Iranian Oil Company
is a contract with the Company for the development of the country's
oil. Thus, as I see it, the present issue is essentially one of
abrogation of contract.

The British Government has placed this 1951 case before
the World Court. As in the 1933 dispute, Iran has denied the
jurisdiction of the Court, contending that the dispute was not
one of International Law, but simply one of local (Iranian) law.
Whether or not Iranian law, when applied to a similar situation
arising between the government and one of its own subjects,
would approve of such conduct is not of interest in this case.
It is relatively unimportant from a global point of view. Suffice
it to say that this aspect of the situation is covered by the
following conclusion in an article by Nicholas R. Doman, appear­
ing in the December 1948 issue of the Columbia Law Review, in
which he concludes:

(Thus)
"Thus, it would appear to be the settled rule that International Law is superior to Municipal Law, and that a state even with the excuse of its constitution cannot evade obligations incumbent upon it by treaty or International Law."

For a further and careful treatise which bears on the entire matter, I refer you to a report on Expropriation of Immovable Property prepared in 1938 by a subcommittee of your own Association.

As a tenet of International Law, the United States, though not approving the practice, has in general recognized the right of a sovereign to nationalize properties within its own borders, even though owned by nationals of other countries provided prompt, adequate and effective compensation is paid, and if pre-existing obligations are not evaded thereby. We have not, to my knowledge, taken the position that there is either a right or a privilege on the part of a sovereign power to breach its contract. It may be that because the judicial remedy is inadequate or the political situation so requires, a sovereign power will escape judicial or other sanction if it violates its agreements, but this is something quite different from recognizing a right to do so. A careful distinction must be made between "the right or privilege to breach a contract" and "the power to breach a contract." Admittedly, nations may have this power, but we must always deny that there is an absolute and unqualified
right or privilege, at least in so far as its incidence on property rights of aliens is concerned. Care should be exercised to avoid the pitfall that "might makes right". That label describes the type of society that we are trying to avoid in our current international relationships.

Governments sometimes claim to act under the name of nationalization in altering or setting aside their contracts. I think this is a failure to distinguish basic legal relationships. The right of a sovereign to nationalize is one thing; but the duties under International Law accruing to a sovereign which has entered into a prior contract binding on itself is quite another thing. To assert that the right of a sovereign to nationalize is superior to its duty under such a binding contract is to misapply fundamental legal concepts.

Regardless of the legalistic concepts, we must all agree that if sovereign governments are going to abrogate contracts unilaterally whenever it suits their purpose, there will be no basis for international commercial relationships. No one knows better than those assembled here this afternoon that faith in some spoken or written contract is a prerequisite to every business deal. International business is no different. The oil industry of Iran was developed by men and money from another country acting on faith in a contract.

The recent request by the Government of India that a refinery be built there by foreign capital shows how meager is the understanding of this basic issue of whether Iran is within its right in cancelling its agreement with the Anglo-Iranian Oil Company.

(The major)
The major amount of the petroleum products required by India in the normal course of trade came from Abadan. With the closing of the refinery at Abadan a temporary shortage of petroleum supplies has developed in India. While this will be corrected in the near future, some time is required to shift channels of trade. India, in requesting foreign oil companies to build a refinery there, stated she would guarantee there would be no nationalization for thirty years.

In 1933 Iran made a similar guarantee, except it was for sixty years. You will recall that Article 21 of the 1933 agreement stated that neither the executive nor legislative branch of the Government would alter or cancel it. Furthermore, this agreement was not only signed by the executive branch, but was ratified by Parliament. If Iran is under no obligation to abide by its agreements, then neither would India nor any other government be required to live up to its agreements. In other words, the day after the refinery was built, India, with the same right as that exercised by Iran, if there be such a right, could unilaterally abrogate the contract which she had made with the foreign companies.

If it should become a principle of International Law that governments cannot make contracts which are legally binding on them, as seems to be the contention of Iran, then on what basis can foreign capital be invested in these countries? How is the Point Four Program to be carried out? Less developed countries need the skill and capital to be supplied by the more advanced countries. By this method we hope to help these nations create (greater wealth;
greater wealth; that is help them create more goods needed for consumption in order to provide a higher standard of living in the world. It is a most desirable objective. We should be careful not to undermine the principle which will make its accomplishment possible.

In the world today we are endeavoring to adopt a higher order of conduct among nations. We are searching for a substitute for armed force that has so often governed in the past. We are contending that the law of the jungle should no longer apply to problems arising among nations any more than it should apply to the problems arising among private persons. This is a higher order of society. It must live by a code of conduct under which rights of nations and individuals engaging in foreign operations are observed. The principles of respect for property rights and the sanctity of contracts are basic in such a code. If the civilized world accepts without protest violation of these principles, the international investment and trade required for the economic well-being of the peoples of the world will be inhibited. The objectives of the President's Point IV Program will be impossible of accomplishment.

Property and contract rights can be and frequently are modified by mutual agreement. The "pound of flesh" approach is not a proper solution to problems which have arisen due to a change in the basic conditions which were present at the time the contract was made. Neither is it proper remedy for one of the parties unilaterally to disregard his solemn engagement. Where, with the passage of time and the appearance of unforeseen (conditions)
conditions, the carrying out of a contract strictly in accordance with its terms would create undue hardship, it may be desirable to change the contract. But if that is to be done, it is essential that both parties to the original contract likewise be parties to the changes. To maintain, as some do, that sovereignty includes the right to set aside such contracts unilaterally is not to exalt sovereignty but to put it in a class with minors who likewise are unable to make binding contracts. Nations which have come of age, like individuals who have attained their majority, recognize the practical value of their contractual powers.

If it be admitted there may be occasions, though few, where contractual obligations should be changed, by what standards are the newer arrangements to be measured? I cannot supply the answer, but I am firmly convinced that most of the problems can be settled by bilateral negotiations provided both parties to the contract are not only willing, but determined, to reach a fair conclusion. This is the pattern that has been followed in the past and is being followed now in respect to some of the foreign concession areas in which oil companies are operating. In understanding such negotiations due regard should be paid both to past commitments and existing circumstances. Should there be a complete failure to agree under these conditions—an eventuality hard to see—then I suppose some new authority is required to settle the matter between the parties. Certainly if we are ever to have a world governed by law rather than by force, we must come to regard it as no more a limitation on a nation's sovereignty
to be required to respect the contracts it has freely made, than we regard it as a limitation on an individual's freedom that he do likewise.

The need for establishing this principle of law as a foundation on which to build our international society is so self-evident, it seems to me, that it requires no explanation. Yet there is hardly a day that passes that I do not see a statement by a prominent political figure or a leading newspaper columnist which shows a lack of understanding of this basic concept. Every effort is made to find expedient solutions of our troubles at the moment. If the solution results in the destruction of faith in the written or spoken word, then harm has been done not only to our other interests, but the solution proposed may be of no lasting benefit.

Lawyers are perhaps best qualified of all groups to understand not only the distinction between these rights but the paramount need for a better understanding by those persons charged with the responsibility of guiding our national interests. I hope you will seize upon every opportunity to help others with whom you come in contact to understand the importance of this issue. If we are to have an intelligent foreign policy, our basic objectives should be clear and our understanding of particular concepts should be sharpened.

Dollars alone cannot cure our problems. The billions and billions of dollars we are spending annually both in building up our own defenses and in aiding other friendly nations will be (of no avail)
of no avail unless, at the same time, we are able to establish a code of conduct covering international relationships which will enable us to live together in a family of nations. Recognition of property rights and the sanctity of contracts is essential. Wherever there is an attempt to violate these principles, then we, as a country, should make it known that we expect any nation to discharge contractual obligations freely made. It is one of the responsibilities that follows our assumption of world leadership.

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