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The Hormuz Tollbooth: How the Flawed Islamabad Agreement Led Back to Gulf Warfare

By

Lāsma Kokina

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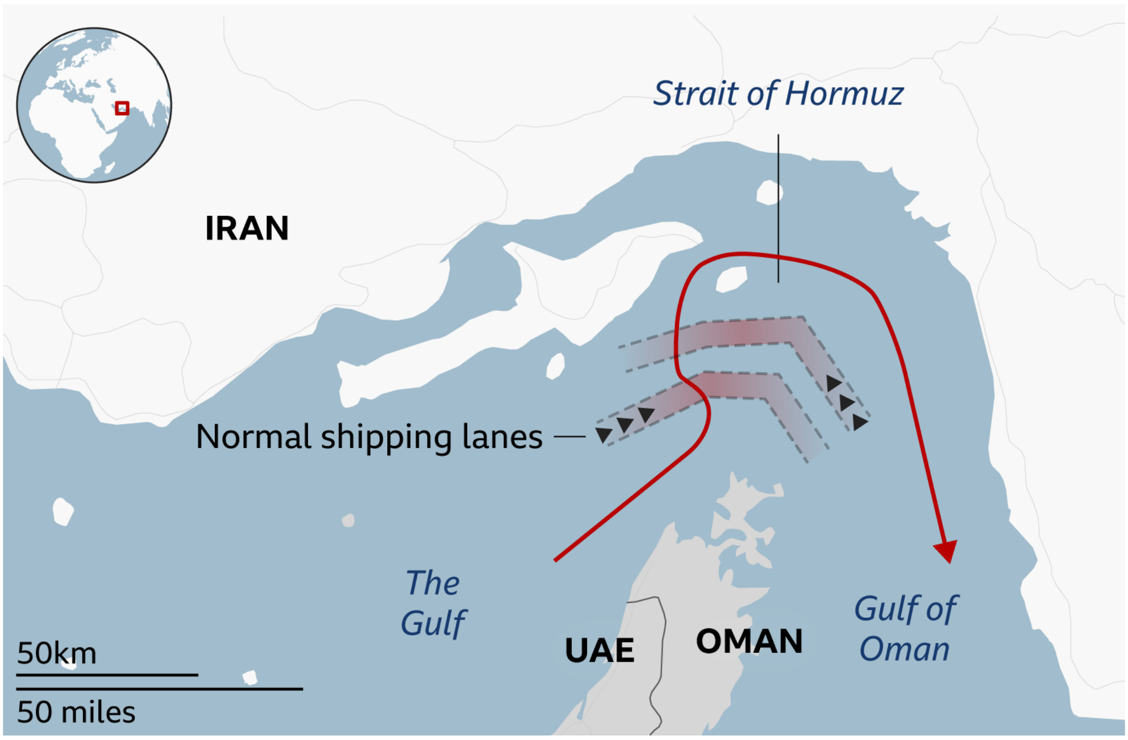
Executive Summary

- Iran established the Persian Gulf Strait Authority in May 2026 to turn the international waterway into a toll zone requiring heavy transit fees paid in cryptocurrency.
- The United States and Iran signed the Islamabad Memorandum of Understanding in June 2026 to pause warfare, but the truce quickly unraveled due to deep disagreements over who would permanently manage the strait after a temporary sixty-day grace period.
- Tehran attempted to build a joint administrative framework with Oman to implement permanent maritime fees, a move that severely strained Oman's traditional neutrality.
- The ceasefire officially ended in early July 2026 after Iranian forces attacked commercial tankers, which prompted a massive wave of retaliatory US counterstrikes against approximately 140 military targets inside Iran.
- Tehran responded by re-closing the Strait of Hormuz and launching a widespread regional missile barrage, though both nations have recently agreed to maintain diplomatic communication through Omani mediation.

Key Picture: Strait of Hormuz Shipping Corridor (Route taken by Pakistan oil tanker)



Source: BBC

Flawed Diplomacy, Toll Regimes, and the Path Back to War

Pre-war, the Strait of Hormuz functioned as a tariff-free international maritime corridor situated between Iran and Oman, facilitating the global distribution of petroleum and natural gas from the Persian Gulf. Since that time, Iranian officials have frequently expressed their desire to generate revenue from the strait.[1] Following its late February 2026 wartime closure, Iran formalised its control on May 18 by launching the Persian Gulf Strait Authority (PGSA). This official state bureaucracy converts the international waterway into a vetted toll plaza, requiring operators to submit a Vessel Information Declaration and pay transit fees up to $2 million in cryptocurrency per voyage, though some fee-less passages can be negotiated bilaterally. Tehran also added a bitcoin-priced maritime insurance program, "Hormuz Safe," which could generate $10 billion annually. In response, the US government sanctioned the PGSA on May 27 and warned against making payments.[2]

To avert a total economic and military meltdown, the US and Iran signed an interim peace framework on June 18, 2026, known as the Islamabad Memorandum of Understanding (MoU).[3] This historic, Pakistan-mediated agreement was designed to immediately pause active warfare, lift the American naval blockade, and establish a sixty-day window of toll-free commercial shipping under Article 5.[4] Digitally signed by the US President President Donald Trump and Iranian President Masoud Pezeshkian, the memorandum promised a gradual lifting of the US naval blockade, the release of frozen Iranian assets, and the establishment of a massive three hundred billion dollar reconstruction fund for Tehran.[5]

However, the situation quickly deteriorated into the latest crisis because Article 5 contained deep structural ambiguities regarding who would permanently manage the strait once that temporary two-month grace period expired. While the US expected an absolute, permanent return to open navigation, Iran interpreted the clause as a mandate to establish sovereign administrative control, leading the Islamic Revolutionary Guard Corps to enforce strict shipping lanes and float mandatory "service fee" regimes.[6]

More specifically, Article 5 of the Islamabad Agreement was ostensibly designed to restore the flow of global commerce through the Persian Gulf. The provision mandated the immediate reopening of the Strait of Hormuz and strictly required Iran to provide safe, toll-free passage for all commercial shipping for a designated sixty-day period. The text assigned Tehran the sole responsibility of demining the strategic waterway within thirty days, pointedly excluding any allowances for multinational naval participation.[7] While Western diplomats celebrated the guaranteed two-month window of free navigation, Iranian officials immediately seized upon the long-term ambiguities of the text. Crucially, the pact left the door open for Iran and the Sultanate of Oman to jointly define the future administration and maritime services in the strait once the sixty-day grace period expired.[8] This fundamental policy clash triggered recent military flare-ups and fresh US airstrikes in the region.[9]

The role of Oman

Almost immediately after signing the agreement, Tehran shocked maritime markets by announcing its intention to implement a permanent system of maritime fees. Iranian First Vice President Mohammad Reza Aref explicitly stated that Tehran would retain absolute control over the Strait of Hormuz, arguing that commercial vessels using the waterway must contribute financially to the costs of services. To strengthen this position, Tehran engaged with its southern neighbor, the Sultanate of Oman, proposing a joint administrative framework.[10]

Oman had submitted a formal proposal to the US and other Western allies outlining a plan to charge shipping companies service fees for using the strait. Oman has a long-standing history of neutrality, frequently acting as an intermediary between Iran and the US. However, escalating regional tensions driven by the war have made this balancing act much more difficult. Following May reports that Oman was considering a joint plan with Iran to collect transit fees in the strait, Donald Trump already reacted by threatening military action, warning Oman to "behave just like everybody else."[11]

What Are the Long-term Consequences of a Permanent "Tehran tollbooth"?

An Iranian toll system in the Strait of Hormuz directly challenges freedom of navigation - a core principle of international law long guaranteed by US naval power. Permitting Tehran to monetise this transit point would mark a major strategic defeat for Washington and destabilise Middle Eastern energy markets, the vital economic engine for Gulf nations like Saudi Arabia, the UAE, and Qatar. Crucially, it would also grant Iran permanent geopolitical leverage to delay, restrict, or block rival shipping at will, turning a key global transit route into a tool for diplomatic coercion.[12]

Additionally, this framework directly conflicts with the UN Convention on the Law of the Sea (UNCLOS), an agreement that guarantees vessels unrestricted transit through over 100 international straits, including the Strait of Hormuz. While roughly 170 nations and the European Union have ratified UNCLOS, establishing it as customary international law, neither Iran nor the US have signed on. Nonetheless, the US explicitly rejects Iran's claims of control over the vital waterway. Compounding this tension is the issue of economic restrictions; because Iran has been entangled in a complex web of US and UK sanctions since the 1970s, major Western shipping corporations are legally barred from making any financial transactions with the Islamic Revolutionary Guard Corps (IRGC).[13]

Potential Costs

Based on pre-crisis flows, a $1 per barrel toll would add $20 million a day to the global market, but the true financial impact of this regime extends far beyond that fee. The de facto closure of the strait cut regional exports by 10 million barrels a day, causing Brent crude to surge toward record highs and driving up shipping costs through elevated freight rates, soaring insurance premiums, and mandatory hazard double-pay for crews. Because damaged infrastructure and limited pipeline capacity make a swift return to pre-crisis volumes unlikely, market analysts predict that this sustained supply squeeze will keep oil prices elevated at around $100 a barrel through 2026 and into 2027. Ultimately, even if Iran permits passage, the combination of high costs, legal complexities, and security threats will likely prompt traders to avoid Gulf crude altogether.[14]

The Toll Failure and the Return to Direct Conflict

Ultimately, the fragile diplomatic effort between Washington and Tehran proved too unstable and Iranian naval forces aggressively resumed their harassment of commercial shipping. In a fatal breach of their core obligations under the memorandum, Iran launched direct attacks on multiple tankers navigating the strait in early July.[15]

The Western response was fast and uncompromising. On July 8, 2026, Trump unequivocally declared that the Islamabad Memorandum was effectively "over", publicly dismissing the Iranian leadership as impossible to negotiate with.[16] After a Cyprus-flagged container ship was struck by Iranian forces and set ablaze in the Strait of Hormuz, the US military launched a massive wave of counterstrikes. US Central Command confirmed hitting roughly 140 military targets inside Iran, including drone launch sites, ammunition dumps, and military assets on Qeshm Island.[17]

In response to the American bombardment, Tehran claimed the Strait of Hormuz was once again fully closed. Simultaneously, Iran launched an expansive missile and drone barrage targeting US assets and regional neighbours, triggering missile defense alerts and interceptions across Bahrain, Qatar, Kuwait, Oman, Jordan, and the United Arab Emirates.[18]

As of recently, amid US demands for a formal guarantee of safe vessel transit, Iranian Foreign Minister Abbas Araghchi and his Omani counterpart met to discuss maritime security in the Strait of Hormuz. This development follows an announcement by US President Donald Trump that, despite recent military escalations and his declaration ending the ceasefire between the US and Iran, both nations have agreed to maintain diplomatic talks.[19]

In mid-July, Iranian Foreign Ministry spokesman Esmaeil Baghaei announced that Iran and Oman have committed to ongoing talks regarding the status of the Strait of Hormuz. Baghaei explained that both nations have resolved to maintain political, legal, and technical communication to build a mutual approach to maritime safety in the waterway. He further noted that future oversight of the strait must be shaped by bilateral consultations between Tehran and Muscat, particularly in light of recent regional developments and the military actions taken by the US and Israel against Iran.[20]

Ultimately, the collapse of the Islamabad Memorandum illustrates how the deep structural ambiguities of Article 5 allowed a temporary peace framework to quickly unravel. By interpreting the temporary grace period as a mandate to establish permanent sovereign control and enforce mandatory shipping fees, Tehran directly challenged international navigation laws and triggered a massive military escalation with the US. While mid-July diplomatic talks between Iran and Oman indicate a mutual desire to navigate future maritime oversight, the region remains trapped in a volatile cycle of conflict. With the Strait of Hormuz once again closed, devastating economic costs mounting, and the brief ceasefire officially declared dead, the fundamental dispute over who controls this critical energy chokepoint continues to threaten global security and regional stability.

NOTES

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