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U.S. AND EU EXPAND SANCTIONS AGAINST IRAN

On June 9, 2010, responding to Iran's continued refusal to suspend its nuclear enrichment program and accept international safeguards, the United Nations Security Council passed Resolution 1929.[1] Among other things, Resolution 1929 banned Iranian investment abroad in nuclear and missile activities, prohibited sales to Iran of arms and proliferation-related items, and established a maritime inspection regime to combat smuggling to and from Iran. Resolution 1929 also urged U.N. member states to take further steps to block the financing of proliferation activities by restricting Iran's dealings with the international banking and insurance industries.

Since that time, the United States, the European Union, and other nations have heeded the U.N.'s call to action and enacted new sanctions against Iran. A number of these measures—particularly U.S. legislation targeting gasoline sales to Iran and investments in Iran's petroleum industry by non-U.S. companies—have extraterritorial implications. Businesses worldwide that are engaged in international trade should therefore be mindful of these new laws' far-reaching provisions.

U.S. LEGISLATION

On July 1, 2010, President Barack Obama signed into law new measures against Iran that had been passed with overwhelming support by the U.S. Congress. Although unlikely to significantly affect U.S. companies, which already are generally prohibited from engaging in virtually all dealings with Iran, these measures, enacted through the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ("CISADA" or the "Act"),[2] primarily seek to pressure non-U.S. companies that conduct petroleum industry-related business with Iran to cease their Iranian activities. The Act aims to accomplish this with a four-fold approach: (1) trying to boost enforcement of existing law targeting non-U.S. companies that invest in Iran's petroleum resources; (2) specifically targeting

1 *Available at* http://www.unhcr.org/refworld/docid/4c1f2eb32.html. All web sites herein last visited on August 25, 2010.

2 *Available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=111_cong_bills&docid=f:h2194enr.txt.pdf.

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companies that do business related to Iran's refined petroleum sector; (3) requiring prospective contractors with the U.S. government to certify that neither they nor any entity they own or control are engaging in sanctionable acts; and (4) authorizing state and local divestment from companies investing in Iran's petroleum industry. In addition, the CISADA strengthens U.S. trade and nuclear sanctions against Iran and establishes additional restrictions against financial institutions' dealings with Iran.

Notwithstanding these new measures, the Act largely preserves the authority of the Executive Branch to waive imposition of the petroleum sector-related restrictions, creating uncertainty as to how and whether any such restrictions actually will be enforced. The Act also permits waiver or delay of numerous other restrictions. Nevertheless, given the broad scope of the Act, as well as Congressional calls for increased enforcement of sanctions on Iran, the prospect remains that some or all of the Act's provisions will be enforced.

Before the CISADA. The United States has imposed sanctions against Iran since the 1979 hostage crisis. Those sanctions in general broadly prohibit U.S. persons from dealing with Iranian companies, individuals in Iran, and the government in Iran. Since 1996, however, the U.S. State Department also has had the authority under the Iran Sanctions Act ("ISA") to impose sanctions against both U.S. companies *and non-U.S. companies* that invest in the development of Iran's petroleum resources above certain monetary threshold levels.

Targeting of Iranian Petroleum Resources Development by the ISA. The ISA required the President to impose at least two out of six possible sanctions on any person—defined to include non-U.S. companies—who made an "investment" of $20 million or more in one year "that directly and significantly contributed to the enhancement of Iran's ability to develop petroleum resources of Iran." The monetary threshold could be met by a single investment or by any combination of investments of at least $5 million each, which, taken together, equaled or exceeded $20 million in any 12-month period. The statute defined "investment" as an equity and royalty arrangement as well as "[t]he entry into a contract that includes responsibility for the development of petroleum resources located in Iran." Notably, the definition specifically excluded "the entry into, performance, or financing of a contract to sell or purchase goods, services, or technology."

Available sanctions under the ISA included: (1) denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports to the sanctioned entity; (2) denial of licenses for exporting U.S. military or militarily useful technology to the sanctioned entity; (3) denial of loans and credits by U.S. financial institutions exceeding $10 million in any 12-month period; (4) prohibition on a sanctioned financial institution's service as a primary dealer in U.S. government bonds, and/or a prohibition on its serving as a repository for U.S. government funds (each counts as one sanction); (5) prohibition on U.S. government procurement from the sanctioned entity; and (6) restrictions on imports from the entity, in accordance with the International Emergency Economic Powers Act ("IEEPA"). The President could waive the application of sanctions by certifying that doing so was "important to the national interest of the United States."

Non-Enforcement of the ISA. When the United States government received credible information that a person had engaged in sanctionable investment activity in Iran, the original ISA called for, but did not require, the President to investigate whether a violation had occurred. Since the ISA's enactment in 1996, the State Department has placed a number of investments in Iran under review, but no sanctions have ever been imposed. In 1997, the United States and the European Union reached an agreement pursuant to which ISA sanctions would be waived as to European entities in exchange for European Union cooperation on nonproliferation and counterterrorism, as well as the European Union's agreement to withhold filing a WTO action based on the ISA's extraterritorial applicability. Nonetheless, the United States made no binding commitment to continue withholding sanctions.

Pressure to Do Something. In recent years, the State Department has encountered increasing Congressional criticism for its failure to enforce the ISA more rigorously,[3]

3 *Available at* http://kirk.house.gov/index.php?option=com_content&task=view&id=3704&Itemid=88.

as media reports highlighted that billions of U.S. government dollars have been sent to companies that have transacted business in Iran's energy sector.[4] Strong legislation intended to force the administration to investigate and impose sanctions under the ISA earned supporters in the 111th Congress, and both houses overwhelmingly passed bills tightening sanctions against Iran and requiring more rigorous enforcement. These measures were consolidated into two larger bills—the Iran Refined Petroleum Sanctions Act (H.R. 2194), which was passed by the U.S. House of Representatives on December 15, 2009 by a vote of 412-12, and the Comprehensive Iran Sanctions, Accountability, and Divestment Act (S. 2799), which was passed by the U.S. Senate by voice vote on January 28, 2010.

The CISADA. Following a conference committee combining H.R. 2194 and S. 2799 into one bill named the Comprehensive Iran Sanctions, Accountability, and Divestment Act, on June 24, 2010, the CISADA was passed by the Senate (99-0) and the House of Representatives (408-8). The President signed the CISADA into law on July 1, 2010. Highlights of the CISADA are as follows:

Refined Petroleum Targeted. The Act takes several steps to restrict exports of refined petroleum to Iran as well as prevent Iran from refining its own petroleum:

- First, the Act adds refined petroleum products, such as gasoline, to the definition of the "petroleum resources" that are subject to the existing prohibition on making investments of $20 million or more that "directly and significantly contribute[ ] to Iran's ability to develop its petroleum resources."
- Second, the Act requires the President, subject to the waiver criteria discussed below, to impose sanctions against a person who "knowingly … sells or provides to Iran refined petroleum products" in the amount of at least $1 million (or $5 million in a 12-month period); or "sells, leases or provides to Iran goods, services, technology, information, or support" that "could directly and significantly contribute to the enhancement of Iran's ability to import refined petroleum products"; or provides transportation, financing, brokering, or insurance for such products, unless the President determines that an underwriter or insurance provider exercised due diligence to ensure it was not supporting such activity.
- Third, the Act requires, again subject to the possibility of waiver, sanctions against any person who "knowingly … sells, leases, or provides to Iran goods, services, technology, information or support" in the amount of at least $1 million (or $5 million in a 12-month period) that "could directly and significantly facilitate the maintenance or expansion of Iran's domestic production of refined petroleum products, including any direct and significant assistance with respect to the construction, modernization, or repair of petroleum refineries."

Change in Knowledge Requirement. The new law broadens the knowledge requirement for sanctionable activity by defining "knowingly" to mean, "with respect to conduct, a circumstance, or a result," that a person "has actual knowledge, or should have known, of the conduct, the circumstance, or the result." Under the preexisting ISA, liability attached if a person engaged in a sanctionable activity "with actual knowledge."

Certification by Government Contractors. The Act requires—unless waived by the President—prospective government contractors to certify, pursuant to new regulations to be issued under the Federal Acquisition Regulation ("FAR"), that neither the contractors nor any entity they own or control engage in activities sanctionable under the ISA.

More Sanctions When the ISA is Enforced. Through a combination of amendments, the CISADA makes more sanctions available under the ISA. First, the Act increases from two to three the minimum number of sanctions that must be imposed by the President under the ISA. At the same time, the Act supplements the six existing sanctions under the ISA with three additional sanctions:

- A prohibition on foreign exchange transactions that are subject to the jurisdiction of the United States;
- A prohibition on transactions between financial institutions, to the extent the transaction is subject to the jurisdiction of the United States and involves any interest of a sanctioned person; and

4 *Available at* http://www.nytimes.com/2010/03/07/world/middleeast/07sanctions.html?_r=2&th&emc=th.

- A prohibition on any transactions in property subject to the jurisdiction of the United States in which a sanctioned person has an interest.

Attempt to Increase ISA Enforcement. The Act seeks to enhance enforcement of the ISA by making it mandatory for the President, upon receipt of credible information, to investigate and make a determination within 180 days whether a person has engaged in sanctionable activity. The Act, however, creates no mechanism to enforce this requirement, and the President could conceivably avoid imposing sanctions by finding a lack of "credible" evidence of ISA-covered activities. The President also need not undertake, and may even terminate, an investigation upon certifying that the person is no longer engaging in the sanctionable activity or has taken significant steps toward stopping it and will not engage in such activity in the future.

For the new refined petroleum sanctions, the requirement of mandatory investigations and determinations is delayed for a period of one year. The Act also permits potential additional delays of 180 days should the President certify that there has been a substantial reduction in sanctionable activities related to refined petroleum during the previous year. The President may seek additional 180-day delays should he certify that there have been progressive reductions of such activities in the intervening period. Thus, the Act gives the President considerable leeway to defer any investigations and determinations related to activities in the refined petroleum sector, possibly indefinitely. Of course, this applies only to the requirement to conduct mandatory investigations. The President may, at any time, investigate and impose the sanctions available to him under the Act.

Narrowed ISA Waiver Criteria. The Act permits the President to waive, for persons in certain countries, application of both the existing and new sanctions only if the President certifies that the country with primary jurisdiction over the person who committed the sanctionable act is closely cooperating with U.S. efforts to prevent Iran's acquisition or development of weapons and that a waiver is "vital" to national security. Whether the new criteria in fact will limit the President's existing discretion in any meaningful way is yet to be determined.

Prohibition on Contracting with Exporters of Sensitive Technology. The Act also prohibits U.S. agencies from contracting with firms that export "sensitive technology" to Iran that could be used to censor or monitor internet usage in Iran.

Authorization of Divestment Measures. The Act specifically authorizes and provides guidelines for certain state and local efforts to divest from investments in companies that do certain business with Iran. The Act also protects asset managers who divest from firms that engage in investment activities in Iran (as well as Sudan).

Trade Sanctions. The Act somewhat tightens U.S. export controls related to Iran and takes aim at countries through which restricted items are believed to be diverted to Iran.

- The Act prohibits all imports from Iran except for "information and informational materials," superseding previous regulations that permitted the importation of carpets, foodstuffs, and gifts of less than $100.
- The Act expands existing bans on U.S. exports to Iran to include all items except food, medicine, and humanitarian assistance; services, hardware, and software for internet communications; informational materials; goods or services for commercial aircraft, the International Atomic Energy Agency, the promotion of democracy, or those deemed "necessary to the national interest."
- The Act targets countries that serve as intermediaries through which restricted exports are diverted to Iran by directing the President to designate any such country a "Destination of Diversion Concern" and requiring a license for certain exports to the country, with a presumption that the license will be denied. The President is permitted to delay the licensing requirement if he determines that the country is taking steps to strengthen its export control system, interdict the diversion of sensitive items, and comply with U.N. Security Council resolutions

Nuclear Materials. The Act prohibits all transfers of nuclear material, pursuant to any cooperation agreements with the United States, to a country with primary jurisdiction over a person who engages in sanctionable activity relating to the acquisition or development of nuclear weapons or delivery systems, unless the President determines that approving such transfers is vital to national security, or that the country

has no reason to know of the activity, or is taking all reasonable steps to prevent a recurrence of the activity and penalize the person.

Financial Institution Sanctions. The Act directs the Secretary of the Treasury to prescribe regulations that restrict the opening or maintaining of a U.S. "correspondent account" or "payable-through account" by a foreign financial institution that knowingly facilitates Iran's efforts to acquire weapons of mass destruction or support terrorism. These regulations also require the domestic institution maintaining such an account to conduct an audit of the foreign institution's activities and certify that to the best of its knowledge, the institution is not knowingly facilitating such activity. The Act also mandates regulations prohibiting entities owned or controlled by domestic financial institutions from knowingly engaging in significant transactions with or benefiting Iran's Revolutionary Guard Corps or its agents and affiliates. The first of these regulations have been issued[5] and became effective on August 16, 2010, authorizing the Secretary to impose "strict conditions" on violators, such as banning the provision of trade finance to the foreign financial institution's account, restricting the transactions that may be processed through it, or prohibiting outright the opening or maintaining of U.S. accounts for a foreign financial institution that knowingly engages in the sanctionable activities. Notably, the regulations also provide for civil penalties of up to the greater of $250,000 or twice the transaction value, as well as potential criminal penalties for willful violations of up to $1 million and 20 years in prison. The Treasury Department may waive the application of these restrictions if it determines such a waiver is necessary to the national interest.

EUROPEAN UNION

Unlike the U.S., the EU has not imposed a blanket sanctions regime on Iran but has instead applied more selective restrictions targeting certain Iranian government entities and goods and services that could be used to develop nuclear weapons and other weapons of mass destruction. In addition, the EU has supported UN resolutions relating to Iran and its nuclear program.

5 *Available at* http://www.ustreas.gov/offices/enforcement/ofac/legal/regs/fr75__49836.pdf.

On June 17, 2010, shortly after the adoption of Resolution 1929, the European Council—comprising the heads of state of each of the EU Member States, the President of the EU, and the President of the Commission—issued a Declaration on Iran, [6] stating that the EU would issue new measures supporting Resolution 1929 and directing that these new measures focus on the areas of trade, especially dual use goods; trade insurance; the financial sector; the Iranian transport sector; and key sectors of the oil and gas industry.

This direction was implemented by the Council of the European Union, the EU legislative body responsible for promulgation of EU foreign policy, in its Decision of July 26, 2010[7] (the "New EU Sanctions"). The New EU Sanctions were immediately effective and applicable to each Member State, its nationals, and to all people and entities within the EU.

New Dual Use Regime. The New EU Sanctions significantly enhance controls over dual use goods. Under Article 1.1(e), *all* dual use goods (other than certain telecommunications and information service goods) now fall within the scope of the EU's Iranian sanctions program, and the direct or indirect supply, sale, or transfer of anything listed in the EU's extensive dual use list is prohibited without special permission.[8] Permission is granted on a case-by-case basis, subject to Member State authorities' satisfaction that the dual use good would clearly not contribute to Iran's development of nuclear weapons, that appropriate end-user certifications were provided, and that the government of Iran provided assurances that the goods will not be used for prohibited activities. Member States are required to inform each other of requests for permission they have refused.

Weapons and Nuclear Development. Article 1 of the New EU Sanctions also prohibits trade with Iran of items that can be used for weapons (including equipment and parts) or prohibited nuclear activities, including the development of nuclear weapons and nuclear weapons delivery systems, enrichment-related reprocessing or heavy water-related

6 *Available at* http://www.ustreas.gov/offices/enforcement/ofac/legal/regs/fr75__49836.pdf.

7 *Available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:195:0039:0073:EN:PDF.

8 *Available at* http://trade.ec.europa.eu/doclib/docs/2009/june/tradoc__143390.pdf.

activities, and "the pursuit of activities about which the International Atomic Energy Agency has expressed concerns or has identified as being outstanding" ("nuclear weapons development").

A catch-all provision in Article 2 states that the export to Iran of goods that might assist in nuclear weapons development (and any technical or financial assistance relating to the export of those goods), even if not specifically mentioned in Article 1, also is subject to case-by-case authorization by Member State authorities.

Petrochemical Sanctions. Article 4 of the New EU Sanctions prohibits the sale, supply, or transfer of "key equipment and technology" (and any related technical or financial assistance) for certain "key sectors" of the Iranian oil and gas industry—the refining, liquefied national gas, exploration, or production sectors—as well as to Iranian or Iranian-owned enterprises engaged in these "key sectors" outside of Iran. This means exporters must ascertain whether any of their customers are ultimately owned by Iranian entities.

Although the phrase, "key equipment and technology" is not defined in the New EU Sanctions, Article 4 indicates that the EU plans to enumerate the "relevant items" covered by the provision in a future measure. Thus, any exporter engaged in these sectors should proceed with caution in exporting any item to Iran.

Transactions concluded before the date of the adoption of the New EU Sanctions are exempt from the prohibitions in Article 4. But performance of a contract that would be permitted under this carve-out may be commercially impossible, given that Article 6 prohibits granting any financial loan or credit to enterprises in Iran that are engaged in any of the "key sectors" or to Iranian or Iranian-owned enterprises engaged in these sectors outside of Iran.

Prohibited Investment in Uranium. Article 5 prohibits Iranian investment in EU entities engaged in any commercial activity relating to uranium mining, production or use of nuclear materials and technology (and in particular uranium enrichment and reprocessing activities), heavy-water-related activities, or technologies relating to ballistic missiles capable of delivering nuclear weapons.

Export Trade Support/Financial Sanctions. The New EU Sanctions contain a number of prohibitions on export trade support to Iran and on any new commitments for grants, financial assistance, and concessional loans to the government of Iran, except for humanitarian and developmental purposes. In order to prevent export assistance in one area from financing nuclear weapons development, the prohibitions on export trade support are general and not limited to nuclear weapons development activities.

The New EU Sanctions also prohibit EU investments and deposits in Iranian banks, the opening of bank accounts in the EU for Iranian banks and Iranian nationals, and the provision of insurance or re-insurance to Iranian entities, entities acting on behalf of Iranian entities, or entities owned or controlled by them.

Enhanced Reporting. The new trade support and financial sanctions are backed up by reporting requirements, which apply at very low financial thresholds. Financial regulators in the applicable Member States must be notified of all nonhumanitarian transfers of funds in excess of €10,000 from Iran to the EU or from the EU to Iran that are routed through an EU financial institution. EU financial institutions must obtain prior authorization from their Member State's government before processing any transaction in excess of €40,000, although such authorization will be deemed granted if the Member State's government does not object within four weeks of an institution's request.

These sanctions are further supported by measures freezing bank accounts and reiterating the EU's existing prohibitions on dealing with certain Iranian nationals and entities, including those recently named in Resolution 1929. The reporting requirements may well turn out to be the provisions of the New EU Sanctions with the most bite.

Transport and Logistics Sanctions. The New EU Sanctions prohibit Iranian cargo planes from landing in the EU and ban EU nationals from bunkering or providing ship supply services or other servicing of vessels to Iranian owners or contracted vessels, unless for humanitarian purposes, until the cargo has been inspected and any goods subject to sanctions removed. The measures also prohibit the provision of engineering and maintenance services to Iranian cargo

aircraft by nationals of Member States. As these prohibitions apply to EU nationals, the sanctions will be breached even if the services are performed outside of the EU.

In addition, Member States are directed to inspect all cargo to and from Iran in their territories if they have reasonable grounds to believe the cargo contains prohibited goods. They are also directed, consistent with international law, to request inspection of vessels on the high seas with the consent of the flag state.

End-User Vigilance. To facilitate enforcement of the New EU Sanctions, most of its provisions, including the Article 1 dual use sanctions, prohibit not only the export of the goods themselves, but also the provision of technical assistance or training, investment, or brokering services related to the sanctioned goods. The New EU Sanctions also prohibit any Member States, nationals, and people and entities within the EU from participating knowingly or intentionally in activities that have the purpose of circumventing the sanctions, or providing sanctioned goods or services to any person, entity, or body in, or for use in, Iran. This means that all exporters must be vigilant as to the ultimate destination of their exports. Even service providers must ensure that they are not providing technical services to someone who will subsequently provide them in Iran.

Article 14 of the New EU Sanctions directs Members States to require their nationals and persons and firms subject to their jurisdiction to exercise vigilance when doing business with entities incorporated in Iran or subject to Iran's jurisdiction, and any entities owned or controlled by them, including through illicit means, in order to ensure that such business does not contribute to nuclear weapons development.

Claims Immunity. One final noteworthy feature of the New EU Sanctions is Article 22, which provides that no claims, including claims for compensation, in connection with a contract or transaction that is directly or indirectly affected by the New EU Sanctions (or, more broadly, by new measures adopted as a result of Resolution 1929) shall be granted to any specified Iranian bodies or to any other person or entity in Iran. While this provision prevents the enforcement of any such awards in the EU, it cannot preclude actions brought outside the EU by Iranian parties, including arbitration claims.

OTHER NATIONS

Although beyond the scope of this update, companies should be aware that several other nations have enacted domestic sanctions as part of similar efforts to implement the measures urged, but not required, by Resolution 1929. Such nations include Australia, which on July 29, 2010 announced "autonomous" sanctions against Iran,[9] and Canada, where the Special Economic Measures (Iran) Act[10] took effect on July 26, 2010. These sanctions regimes also can have very broad reach, given that they are designed, like the U.S. and EU measures, to hinder Iran's development of nuclear, chemical, biological, and missile programs, and to persuade Iran to return to international negotiations.

CONCLUSION

It is difficult to predict what effect, if any, these new sanctions will have on Iran. In the past, the Iranian government has claimed to be impervious to sanctions on gasoline imports, having recently expanded its domestic refining capacity,[11] reduced demand by eliminating gasoline subsidies, and secured contracts with suppliers in India, Turkmenistan, China, and the Netherlands. But while Russia, India, and China have indicated they will not abide by the new U.S. sanctions, early reports suggest that Iranian shippers are struggling to find insurance, as Western insurance companies cut ties with Iran in preemptive compliance with the CISADA and in compliance with the New EU Sanctions.[12] Development of Iran's massive South Pars natural gas reservoir has been hampered as well by the withdrawal of Western firms.[13]

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9 *Available at* http://www.dfat.gov.au/un/unsc_sanctions/iran_autonomous_sanctions.html.

10 *Available at* http://canadagazette.gc.ca/rp-pr/p2/2010/2010-08-04/html/sor-dors165-eng.html.

11 *Available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/06/23/AR2010062303770.html?hpid=topnews.

12 *Available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/07/20/AR2010072005958.html?hpid=sec-world.

13 *Available at* http://www.washingtonpost.com/wp-dyn/content/article/2010/07/22/AR2010072203933.html?hpid=moreheadlines.

What is clear, however, is that strict enforcement of the CISADA and the New EU Sanctions would have significant repercussions for the international business community. Moreover, effective compliance programs, including diligent identification of customer and end-user intentions, will be more important than ever for companies engaged in international trade.

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