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New U.S. Legislation Targeting Activities of Non-U.S. Firms in Iran Has Broad International Implications

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The United States has enacted legislation that amends and significantly expands the Iran Sanctions Act of 1996 (the “ISA”).

What Is New

The Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 amends the ISA to create additional categories of activities that could subject non-U.S. firms to sanctions, and it creates new types of sanctions that can be imposed on such firms. The new activities subject to sanctions include those that support the production of refined petroleum products in Iran and the importation of refined petroleum products into Iran. Also, the new legislation targets foreign financial institutions that facilitate Iran’s nuclear program, its support for terrorism, or the activities of Iran’s Islamic Revolutionary Guard Corps.

The Context

Iran has faced longstanding criticism and economic sanctions from the United States as both a state sponsor of terrorism and for its alleged nuclear weapons program. Since 1995, the United States has maintained comprehensive sanctions against Iran that prohibit U.S. companies and persons from exporting to, importing from, or investing in Iran. Many Iranian entities are also targeted under U.S. economic sanctions against persons

involved in the proliferation of weapons of mass destruction. The United States has consistently sought to convince the international community to strengthen these multilateral sanctions, and these efforts have recently borne fruit in new measures in the UN Security Council and the European Union. (Click [here](#) to read O'Melveny's June 22 alert on this matter.) Independently of such developments in the international community, the new amendments to the ISA seek to further isolate Iran.

The Implications

While U.S. companies have long been significantly restricted as to activities in Iran, the new restrictions could affect their operations through non-U.S. subsidiaries or affiliates and non-U.S. business partners and competitors. The legislation categorizes additional activities as sanctionable, adds new types of sanctions, mandates investigations into credible reports of sanctionable activity, and constrains the President's authority to waive sanctions.

Further Information Concerning the New Legislation

The ISA applies to any person, including non-U.S. persons, but primarily targets non-U.S. persons because U.S. persons are already prohibited from investing or trading with Iran under other U.S. economic sanctions programs. Under the ISA, sanctions are imposed if an investigation concludes that prohibited activity occurred. The President, however, can waive the sanctions and in fact has done so in the past.

The Comprehensive Iran Sanctions, Accountability, and Divestment Act (the "Amendments") creates additional categories of sanctionable activity and new types of sanctions.

Activity Subject to Sanctions

Prior to the Amendments, the ISA targeted investments of US\$20 million or more "that directly and significantly contributed to the enhancement of Iran's ability to develop petroleum resources of Iran." Now, the ISA potentially sanctions persons that "knowingly" engage in activities that could "directly and significantly" facilitate or contribute to Iran's domestic production of refined petroleum products or Iran's ability to import such products, if such activities exceed a fair market value of US\$1 million or more or an aggregate fair market value of US\$5 million or more in a 12-month period. Specifically, the Amendments potentially sanction the sale, lease, or provision to Iran of:

- "goods, services, technology, information, or support 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"; and

- refined petroleum products or “goods, services, technology, information, or support that could directly and significantly contribute to the enhancement of Iran’s ability to import refined petroleum products,” including activities such as underwriting, insuring, reinsuring, financing, brokering, or providing ships or shipping services.

There is an exception for underwriters and insurance providers who exercise due diligence to ensure that they do not underwrite or contract to insure or reinsure prohibited activities.

Investigations

Until now, the ISA has directed that the President “should initiate” an investigation upon receiving credible information about violations and “should determine” if a person has engaged in the prohibited investment activity within 180 days of the initiation of the investigation. Going forward, the ISA requires that the President “shall initiate” an investigation and then “shall” make a determination.

Menu of Sanctions

If the President determines that a person engaged in specified activities is subject to sanctions, the President must select from a menu of sanctions, absent a Presidential waiver. The ISA previously required the President to impose at least two of the following six sanctions:

- denial of Export-Import Bank loans, credits or guarantees;
- denial of licenses to export military or militarily useful technology;
- prohibition on U.S. financial institutions making loans or providing credit of more than US\$10 million in any twelve-month period (with minor exceptions);
- prohibition on obtaining U.S. Government procurement contracts;
- restrictions on imports into the United States; and
- if the violator is a financial institution, prohibition on being designated as a primary dealer in U.S. Government debt and/or prohibition on acting as an agent for U.S. Government funds.

The Amendments add three new sanctions to this menu and require the President to select at least three of the nine sanctions now available. The new sanctions options would prohibit:

- foreign exchange transactions in the United States;
- transfer of credits or payments by financial institutions in the United States; and
- dealings in property in the United States.

Waiver Authority

The Amendments both narrow and broaden the President’s waiver authority. Since the ISA was enacted, no President has imposed sanctions and President Clinton exercised his discretion to waive such sanctions in one instance. The law required the President to certify that a waiver was

“important to the national interest of the United States.” Going forward, the standard for waiver is higher: the President must certify that a waiver is “necessary to the national interest.”

The Amendments provide an additional avenue for waiver in certain circumstance, however. The President may waive sanctions with respect to persons from countries that cooperate in multilateral efforts concerning Iran. For up to 12 months (renewable under certain circumstances), the President may waive the imposition of sanctions if the government with primary jurisdiction over the person subject to sanctions “is closely cooperating with the United States in multilateral efforts to prevent Iran” from acquiring or developing chemical, biological, nuclear, or certain advanced conventional weapons and if doing so is “vital to the national security interests.” It is contemplated that this waiver authority permits the President to waive sanctions against EU firms, and firms from other countries that have cooperated with U.S. efforts vis-à-vis Iran.

Expanded Definitions of Person and Petroleum Resources

The Amendments expand the definition of “person” to include financial institutions, insurers, underwriters, guarantors, and other business organizations. “Petroleum resources” is now defined to include “petroleum, refined petroleum products, oil or liquefied natural gas, natural gas resources, oil or liquefied natural gas tankers, and products used to construct or maintain pipelines used to transport oil or liquefied natural gas.”

Potential Restrictions on Government Procurement

The Amendments require prospective government contractors to certify that they do not engage in any of the above-described energy sector activities subject to sanctions. Contractors that submit false certifications are subject to debarment. Effectively, this requires foreign companies to cease such sanctionable activities in order to remain eligible for government contracts. The Amendments also prohibit federal procurement contracts with persons that export technology to Iran that is intended to restrict free speech in Iran.

Effective Date

The Amendments take effect immediately. The Amendments provide a one-year grace period for the launching of investigations of persons engaging in activities related to the production or importation of refined petroleum products, however. Such persons are subject to investigation only for sanctionable activities that commence on the one-year anniversary date of the Amendment’s enactment, or thereafter.

Financial Institutions

The foreign subsidiaries of domestic financial institutions are barred from knowingly engaging in transactions that benefit Iran’s Revolutionary Guard Corps or its agents or affiliates whose property is blocked pursuant to the International Emergency Economic Powers Act. If a foreign subsidiary

engages in such prohibited activities, and the domestic parent has knowledge of such infractions, the parent company itself may be subject to civil and criminal penalties.

Foreign financial institutions may not maintain correspondent and payable-through accounts in the United States if such institutions:

- have engaged in activities that facilitate the Government of Iran (including Iran's Revolutionary Guard Corps and its agents), the Central Bank of Iran, other Iranian financial institutions, or UN-sanctioned persons in developing weapons of mass destruction or supporting foreign terrorist organization; or
- have facilitated significant transactions or provided significant financial services for Iran's Revolutionary Guard Corps or Iranian financial institutions sanctioned under the International Emergency Economic Powers Act in connection with weapons of mass destruction or support for international terrorism.

In turn, domestic financial institutions that maintain correspondent and payable-through accounts for foreign financial institutions must:

- perform an audit of prohibited activities (as identified in the two preceding paragraphs) that may be carried out by the foreign financial institution;
- report to the Department of the Treasury regarding financial services provided with respect to prohibited activities;
- certify that the foreign financial institution is not knowingly engaging in prohibited activities; and/or
- establish due diligence policies, procedures, and controls to detect whether the Treasury Secretary has found the foreign financial institution to knowingly engage in prohibited activities.

With these provisions, the Amendments delegate a significant responsibility to domestic financial institutions in the implementation of the sanctions on foreign financial institutions.

O'Melveny & Myers has significant depth of experience in the economic sanctions and export controls areas. Its lawyers are actively engaged in conducting internal investigations and transactional due diligence; responding to criminal and regulatory enforcement inquiries and proceedings; evaluating and implementing compliance programs; and providing prospective advice about economic sanctions and export control issues in international business transactions. Our clients include U.S. and international companies, among them Fortune 100 companies, the world's largest financial institutions, and diversified U.S. and offshore companies.