

CLIENT ALERT

Are You At Risk Under Dramatic Expansion of U.S. Sanctions Against Iran and Syria?

August 15, 2012

The United States has dramatically expanded the breadth and scope of sanctions against Iran in two separate actions over the last several weeks. First, President Obama issued Executive Order 13622 prohibiting foreign financial institutions conducting certain transactions with the National Iranian Oil Company or Naftiran Intertrade Company from maintaining accounts in the United States. Second, earlier this week President Obama signed the Iran Threat Reduction and Syria Human Rights Act of 2012 (the "Act"), substantially limiting his discretion under existing sanctions and imposing numerous new provisions with potentially profound effects on the responsibilities for U.S. and non-U.S. companies, alike.

I. H.R. 1905

Most notably, the Act penalizes U.S. parent companies for violations of their foreign subsidiaries, imposes SEC reporting requirements on U.S. companies for the action of their foreign affiliates, and authorizes the President to impose a range of new sanctions against U.S. and non-U.S. companies as well as their corporate officers and principals, for a series of new activities. The following represents a non-exhaustive summary of several of the key provisions in the new legislation.

A. New and Mandatory Sanctions under ISA/CISADA (Section 204)

First, the Act limits the President's preexisting discretion under Section 6(a) of the Iran Sanctions Act (ISA) of 1996, as amended, and the Comprehensive Iran Sanctions, Accountability and Divestment Act of 2010 (CISADA), which both apply to all persons, including solely foreign entities, mandating the imposition of five, instead of three, penalties for previously identified activities. The Act also adds the following to the list of triggers mandating sanctions:

- Joint Ventures with Iran relating to developing petroleum resources outside of Iran if the Government of Iran is a substantial partner or investor;
- Support for the development of petroleum resources and refined petroleum products with an aggregate yearly value of \$5,000,000 or more;
- The provision of goods, services, technology or support which could "directly and significantly contribute" to the maintenance or enhancement of Iran's ability to develop domestic petroleum resources or its domestic production of refined petroleum products;
- The development and purchase of petrochemical products from Iran with an aggregate market value of \$1,000,000 or more in one year;
- The transportation of crude oil from Iran to another country;
- The concealment of Iranian origin of crude oil and refined petroleum products;
- The exportation, transfer, or transshipment of goods, services, technology or other items that would likely result in another person exporting, transferring, transshipping items to Iran that would materially contribute to its ability to acquire or develop weapons of mass destruction; and

- Joint ventures with Iran involving any activity relating to the mining, production or transportation of uranium anywhere in the world.

In addition, the Act adds three new sanctions (Section 204) to the nine sanctions authorized by ISA and CISADA. The President is now permitted to:

- a. prohibit any U.S. person from investing in or purchasing significant amounts of equity or debt instruments of a sanctioned person;
- b. deny visas and exclude from the United States any alien that the President determines is a corporate officer or principal of, or a shareholder with a controlling interest in, a sanctioned person; and
- c. impose ISA/CISADA sanctions on the principal executive officers of any sanctioned person, or on persons performing similar functions or with similar authorities as such officers.

B. Sanctions on Insurers & Reinsurers (Section 212)

Second, the Act expands mandatory sanctions on the insurance and reinsurance industry, requiring the President to impose five or more of the ISA sanctions against persons knowingly providing underwriting services or insurance or reinsurance for the National Iranian Oil Company (NIOC) or National Iranian Tanker Company (NITC) or a successor entity to either such company. These sanctions will be problematic for entities that in the past provided (re)insurance to these entities and that may still be faced with claims relating to those entities. It is unclear whether licensing options will be available to address these circumstances. However, if the President determines the person exercised due diligence in establishing and enforcing official policies, procedures and controls to ensure that the person does not provide those services for NIOC, NITC or a successor entity, the imposition of sanctions is not mandatory. Further, the President may not impose sanctions on persons for providing services involving food, medicine, medical devices or humanitarian assistance to Iran and its people.

C. Liability of Parent Companies for Violations of Sanctions by Foreign Subsidiaries (Section 218)

The Act reverses long-standing U.S. practice and explicitly sanctions U.S. parent companies for the actions of foreign subsidiaries. Invoking the extraterritorial concepts of the Trading with the Enemy Act, the President is now required: (1) to prohibit entities that are (2) owned or controlled by a U.S. person and (3) established or maintained outside the United States, from (4) knowingly engaging in any transaction, directly or indirectly with the Government of Iran, if (5) a U.S. person would be prohibited from conducting the same transaction pursuant to rules promulgated under the authority of the International Emergency Economic Powers Act ("IEEPA")(50 U.S.C. 1701). The "entity" includes any partnership, association, trust, joint venture, corporation or other organization owned or controlled by the U.S. person. In practice, this provision exposes U.S. firms to civil penalties for the actions of their subsidiaries; if after 60 days, a firm's foreign subsidiary violates, attempts to violate, or causes a violation of any sanctions against Iran issued under IEEPA, the parent company will be liable. The Act does provide for a "grace period," exempting a U.S. person from sanctions if it can demonstrate that it has divested or terminated its business with the offending entity within 180 days.

D. Disclosures to the Securities and Exchange Commission Relating to Sanctionable Activities (Section 219)

Finally, all companies required to file reports with the Securities and Exchange Commission ("SEC") are now subject to a new mandatory reporting requirement. Specifically, reporting companies are required to publicly disclose in their quarterly or yearly filings whether they, or any of their affiliates, knowingly engaged in activities prohibited by the following:

- Section 5 of the ISA imposing sanctions on entities engaged in transactions with Iran's petroleum sector;
- Section 104(c)(2) of CISADA imposing mandatory financial sanctions on financial institutions engaged in certain Iran-related transactions;
- Section 105A(b)(2) of CISADA related to weapons and technology used for human rights violations; and
- Executive Orders 13224, blocking property and prohibiting transactions with persons committing terrorism, Executive Order 13382, blocking property of weapons of mass destruction proliferators, and the Iranian Transaction Regulations (ITR).

If the issuer, or its affiliate, is engaged in any of these activities it is required to disclose: (a) the nature and extent of the activity, (b) the gross revenue and net profits related to the activity, and (c) its future intentions regarding continuing the activity. Upon receiving a report disclosing such activity, the President is required to initiate an investigation under ISA and CISADA and issue a determination within 180 days.

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II. Executive Order 13622

On July 31, 2012, President Obama issued Executive Order (E.O.) 13622, "Authorizing Additional Sanctions with Respect to Iran." The E.O. authorizes Treasury to impose new financial sanctions on foreign financial institutions found to have knowingly conducted or facilitated certain significant financial transactions with the National Iranian Oil Company (NIOC) or Naftiran Intertrade Company (NICO), or any entities owned, controlled by, or acting on behalf of NIOC or NICO, for the purchase or acquisition of petroleum, petroleum products, or petrochemical products from Iran. These entities would be prohibited from opening or maintaining correspondent or payable-through accounts in the U.S. In addition, the E.O. authorizes Treasury to block the property and interests in property of any person determined to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services in support of, NIOC, NICO, or the Central Bank of Iran, or the purchase or acquisition of U.S. bank notes or precious metals by the Government of Iran.

Because OFAC has not issued corresponding regulations including general licenses, a number of typically generally licensed activities if conducted with NIOC, NICO and the Central Bank of Iran can now result in sanctionable activity. For example, specific authorization is now needed from OFAC before any person provides mail or telecommunications services to NIOC, NICO, or the Central Bank of Iran. Additionally, any intellectual property claims involving these entities also must be specifically licensed by OFAC – as must the provision of legal services. While these changes again reshape the sanctions landscape with respect to Iran, companies cannot expect a lengthy compliance grace period. Companies must therefore act quickly to assess their current operations, including those of their foreign subsidiaries and affiliates, and develop immediate plans to bring themselves into compliance. Given the lack of corresponding regulations, when in doubt, it may be appropriate to file requests for guidance and specific authorizations.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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