

ECONOMIC SANCTIONS UPDATE

August 2, 2012

Additional Measures Taken by the United States to Further Tighten and Intensify Sanctions With Respect to Iran: New Executive Order

On July 31, 2012, the United States through an Executive Order issued by President Obama (the "EO"), concerned agencies of the U.S. government in charge of imposing, administering and enforcing sanctions, gained legal authority to impose additional sanctions with respect to an expanded category of activity involving Iran. The new EO is effective as of July 31, 2012.

The new EO gives new sanctions powers to both the U.S. Department of the Treasury and the U.S. Department of State. The new EO authorizes the imposition of 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 for the purchase or acquisition of petroleum or petroleum products from Iran through any channel. In addition, the new EO provides new authority to impose sanctions on foreign financial institutions found to have knowingly conducted or facilitated significant transactions for the purchase or acquisition of petrochemical products from Iran. Finally, the new EO provides authority for the U.S. 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.

On July 31, 2012, President Obama stated the following in connection with the new EO:

First, I have approved a new Executive Order that imposes new sanctions against the Iranian energy and petrochemical sectors. This action is designed to deter Iran from establishing payment mechanisms for the purchase of Iranian oil to circumvent existing sanctions, and utilizes the existing structure of our sanctions law, including exceptions for significant reductions in the purchase of Iranian oil. Additionally, existing sanctions on Iran's petrochemical industry are expanded by making sanctionable the purchase or acquisition of Iranian petrochemical products. Sanctions are also authorized for those who may seek to avoid the impact of these sanctions, including against individuals and entities that provide material support to the National Iranian Oil Company, Naftiran Intertrade Company, or the Central Bank of Iran, or for the purchase or acquisition of U.S. bank notes or precious metals by the Government of Iran.

Second, we have also taken a significant step to hold responsible institutions that knowingly enable financial transactions for designated Iranian banks. The Department of the Treasury today imposed sanctions on Bank of Kunlun in China and Elaf Islamic Bank in Iraq under the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA). Bank of Kunlun and Elaf Islamic Bank have facilitated transactions worth millions of dollars on behalf of Iranian banks that are subject to sanctions for their links to Iran's illicit proliferation activities. By cutting off these financial institutions from the United States, today's action makes it clear that we will expose any financial institution, no matter where they are located, that allows the increasingly desperate Iranian regime to retain access to the international financial system.

The three numbered sections below in bold specifically summarize the new categories of activities under the new EO which may lead to the imposition of sanctions.

I. The new EO authorizes the U.S. Treasury Department, with certain exceptions, to impose sanctions on a foreign financial institution that has knowingly conducted or facilitated any significant financial transaction:

(i) with the National Iranian Oil Company (NIOC) or Naftiran Intertrade Company (NICO);

(ii) for the purchase or acquisition of petroleum or petroleum products from Iran; or

(iii) for the purchase or acquisition of petrochemical products from Iran.

For the above-mentioned sanctionable activities, the U.S. Treasury Department may prohibit the opening, an prohibit or impose strict conditions on the maintaining, in the United States of a correspondent account or a payable-through account by a foreign financial institution. Sanctions, however, shall not apply if the country with primary jurisdiction over the foreign financial institution has decreased its oil purchases and imports from Iran. Sanctions shall also not apply with respect to any person conducting or facilitating a transaction for the sale of food, medicine, or medical devices to Iran or when the underlying transaction has been authorized by the U.S. Treasury Department.

II. The new EO, subject to a few narrow exceptions, also authorizes the imposition of sanctions on persons (individuals and entities) that:

(i) knowingly, on or after July 31, 2012, engaged in a significant transaction for the purchase or acquisition of petroleum or petroleum products from Iran;

(ii) knowingly, on or after July 31, 2012, engaged in a significant transaction for the purchase or acquisition of petrochemical products from Iran;

(iii) is a successor entity to a person engaging in the activity mentioned above;

(iv) owns or controls a person determined to have engaged in the activity above, and had knowledge that the person engaged in such activities; or

(v) is owned or controlled by, or under common ownership or control with, a person determined to have engaged in the sanctionable activities above, and knowingly participated in the sanctionable activities.

The sanctions available under the new EO for the sanctionable activities engaged in described immediately above include:

(a) denial of U.S. Export-Import Bank shall deny approval of the issuance of any guarantee, insurance, extension of credit;

(b) a ban on the issuance of any U.S. export licenses to the sanctioned person;

(c) with respect to a sanctioned person that is a financial institution:

(i) the termination or ban on the continuation of any prior designation of, the sanctioned person as a primary dealer in United States Government debt instruments; or

(ii) a ban on the sanctioned person from serving as an agent of the United States Government or serving as a repository for United States Government funds; or

(d) a ban on U.S. Government procurement contract with the sanctioned person.

Additional sanctions may include:

(i) a prohibition on any United States financial institution from making loans or providing credits to the sanctioned person totaling more than \$10,000,000 in any 12-month period, unless such person is engaged in activities to relieve human suffering and the loans or credits are provided for such activities;

(ii) a prohibition on any transactions in foreign exchange that are subject to the jurisdiction of the United States and in which the sanctioned person has any interest;

(iii) a prohibition on any transfers of credit or payments between financial institutions or by, through, or to any financial institution, to the extent that such transfers or payments are subject to the jurisdiction of the United States and involve any interest of the sanctioned person;

(iv) the blocking of all property and interests in property that are in the United States, that come within the United States, or that are or come within the possession or control of any United States person, including any foreign branch, of the sanctioned person; or

(v) a restriction or prohibition on imports of goods, technology, or services, directly or indirectly, into the United States from the sanctioned person.

III. Under the new EO, sanctions may also be imposed on a person that has 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.

The sanctions for the activity described in the paragraph above would block the property and interest in property of the sanctioned person.

The new EO also cuts off donations of any kind to persons on whom sanctions are imposed pursuant to the new EO.

Exception: The new EO provides that sanctions shall not be imposed with respect to any person for conducting or facilitating a transaction involving a natural gas development and pipeline project initiated prior to the effective date of this order to bring gas from Azerbaijan to Europe and Turkey in furtherance of a production sharing agreement or license awarded by a sovereign government other than the Government of Iran before the effective date of this order.

Definitions

Under the new EO:

- the term "petroleum" (also known as crude oil) means a mixture of hydrocarbons that exists in liquid phase in natural underground reservoirs and remains liquid at atmospheric pressure after passing through surface separating facilities;
- the term "petroleum products" includes unfinished oils, liquefied petroleum gases, pentanes plus, aviation gasoline, motor gasoline, naphtha-type jet fuel, kerosene-type jet fuel, kerosene, distillate fuel oil, residual fuel oil, petrochemical feedstocks, special naphthas, lubricants, waxes, petroleum coke, asphalt, road oil, still gas, and miscellaneous products obtained from the processing of: crude oil (including lease condensate), natural gas, and other hydrocarbon compounds. The term does not include natural gas, liquefied natural gas, biofuels, methanol, and other non-petroleum fuels; and
- the term "petrochemical products" includes any aromatic, olefin, and synthesis gas, and any of their derivatives, including ethylene, propylene, butadiene, benzene, toluene, xylene, ammonia, methanol, and urea.

The New EO is in Addition to Existing U.S. Sanctions Laws Applicable to U.S. Persons

The New EO is in addition to existing U.S. sanctions laws applicable to U.S. persons, has extraterritorial effect, and is designed to further deter non-U.S. persons (persons outside the general jurisdiction of the United States) from dealing with Iran. As noted above, the imposition of available sanctions may be

waived with respect to certain non-U.S. persons whose governments have reduced their imports of Iranian oil.

The Impact of the New EO on Maritime Transportation and Insurance

U.S. entities (U.S persons) as well as transactions within the United States, are already subject to the full array of U.S prohibitions governing sanctions against Iran. U.S. insurers are prohibited from covering vessels trading with Iran in the absence of authorization from OFAC. Although, the new EO does not explicitly provide for the imposition of sanctions against shipowners/members that are not U.S. persons, the activities described in Section III. above could be construed to cover shipowners – transportation services in support of, for example, crude oil exported/sold by NIOC. The new EO also is also not clear on whether the transportation or lifting of petroleum, petroleum products or petrochemical products from Iran *per se* would constitute sanctionable activity. OFAC has informally confirmed that the sanctions in Sections I. and II. above would not apply to shipowners or insurers and has also issued the following guidance which may have shed some light on this issue:

These new measures further strengthen the existing comprehensive Iran sanctions framework by deterring work-around financial transactions involving NIOC or NICO that were not being captured under the sanctions previously implemented against the CBI. Iranian trade partners can continue to buy petroleum and petroleum products from Iran without risking sanctions under this E.O. if they have received a significant reduction exception under the NDAA. However, in jurisdictions that do not have a significant reduction exception, the purchase of petroleum or petroleum products and significant dealings with NIOC or NICO may be subject to sanctions under this E.O.

Given the backdrop and the context within which the new EO was issued and previous U.S. government announcements that transportation of petroleum, and petroleum products *per se* were not sanctionable, it is expected that the likely that the focus of the new EO is more on the activities of financial institutions and other actors rather than shipowners and vessels and their transportation of cargo from Iran. OFAC's interpretation makes clear that Iranian trade partners can continue to buy (and ostensibly transport and insure) petroleum and petroleum products from without risking sanctions if they have received waivers from sanctions (imposable on financial institutions) because they have significantly reduced their purchases from NIOC or NICO. However, OFAC has also informally indicated that transporting crude oil sold by NIOC could be viewed to fall within the activities described in section III. above. Whether OFAC will formally and actually adopt such an interpretation is not yet known.

In any event, readers are reminded that EU sanctions against Iran, Council Regulation (EU) No 267/2012 of 23 March 2012 concerning restrictive measures against Iran (the "March 23, 2012 Regulation") prohibits the transportation of crude oil from Iran. The March 23, 2012 Regulation prohibits the importation of Iranian oil or petroleum products into the EU. The March 23, 2012 Regulation, *inter alia*, also prohibits the transportation of crude oil originating in or being exported from Iran to any other

country. Moreover, it prohibits the provision, directly or indirectly, of financing or financial assistance, including financial derivatives, as well as of insurance and re-insurance related to the import, purchase or transport of crude oil and petroleum products of Iranian origin or that have been imported from Iran.

As provided for in exceptions set forth in the March 23, 2012 Regulation, the foregoing prohibitions did not apply to the execution until 1 July 2012, of trade contracts concluded before 23 January 2012, or of ancillary contracts necessary for the execution of such contracts. This grace period has now expired and the prohibitions are now in full force. Additionally, the grace period dealing with insurance and re-insurance (directly or indirectly, of third party liability insurance and environmental liability insurance and reinsurance) related to the import, purchase or transport of crude oil and petroleum products of Iranian origin or that have been imported from Iran also expired on 1 July 2012.

U.S. persons subject to the Iranian Transactions Regulations, are already prohibited (prior to the new EO) from providing cover for vessels lifting crude oil or other petroleum products from Iran, and most U.S. persons in the insurance sector, as a matter of policy, also do not provide cover for transportation that is prohibited by EU sanctions against Iran.

New Sanctions Targets Designated

On July 31, 2012, the U.S. Department of the Treasury announced the imposition of sanctions against two financial institutions (pursuant to legal authority preceding the new EO) for knowingly facilitating significant transactions or providing significant financial services for designated Iranian banks. The financial institutions sanctioned on July 31 by the U.S. Treasury's Office of Foreign Assets Control (OFAC) are Bank of Kunlun in China and Elaf Islamic Bank in Iraq.

The OFAC action against Bank of Kunlun and Elaf Islamic Bank effectively bars them from directly accessing the U.S. financial system. As a result of the sanctions of the type imposed against Bank of Kunlun and Elaf Islamic Bank, financial institutions may not open correspondent or payable-through accounts for Bank of Kunlun or Elaf Islamic Bank in the United States and any financial institutions that currently hold such accounts must close them by August 10, 2012.

More U.S. Iran Sanctions are Imminent

On August 1, 2012, the U.S. Congress approved new legislation (H.R. 1905) providing for punishing new sanctions targeting Iran's energy and shipping sectors. The U.S. House of Representatives voted overwhelmingly 421-6 for the measure. The round of sanctions, which target any person or company which works with Iran's petroleum or natural gas sector, provides insurance to the National Iranian Oil Company, engages in uranium mining with Iran, or sells oil tankers to Iran, passed the U.S. Senate by a unanimous consent vote, and is now on its way to President Obama for his signature whereupon it will become law.

This legislation which is expected to be signed into law provides for, among other things, the imposition of sanctions against any person that knowingly provides a vessel, insurance or reinsurance, or any other shipping service for the transportation to or from Iran of goods that could materially contribute to the activities of the Government of Iran with respect to the proliferation of weapons of mass destruction or support for acts of international terrorism. The Act provides for the blocking and prohibition of all transactions in all property and interests in property of sanctioned persons, if such property and interests in property are in the United States, come within the United States, or are or come within the possession or control of a United States person. Further details on this new legislation will be provided once it becomes law.

It remains to be seen whether, for example, the lifting and transportation of oil or petrochemicals from Iran (and insurance of vessels transporting petroleum or petrochemical cargoes from Iran) will be considered to constitute activity that could materially contribute to the activities of the Government of Iran with respect to the proliferation of weapons of mass destruction or support for acts of international terrorism, and thus be sanctionable.

Compliance and Due Diligence

Given the number and complexity of U.S. laws governing U.S. sanctions against Iran which are cumulative and provide for comprehensive prohibitions and the imposition of sanctions against a wide range of non-U.S. persons trading with Iran, and the constantly evolving rules, the U.S. Iran sanctions net is very large and fine. Thus, the risk that a transaction or activity involving Iran or an Iranian entity will implicate U.S. prohibitions or trigger the imposition of U.S. sanctions at any given time is high. Ambiguities in the law make this risk higher.

Legal determinations as to whether a transaction is permitted or whether it constitutes sanctionable activity are very fact-sensitive. Members are therefore urged to exercise a high degree of caution and due diligence and to obtain competent legal guidance related to their activities involving Iran in order to avoid the imposition of sanctions as well as violations of law.

Questions and Guidance

The Eren Law Firm will continue to very closely monitor the new EO's interpretation and implementation by the designated agencies of the U.S. Government. The Eren Law Firm will continue to interface with the policy-making as well as the enforcement offices of the U.S. government to address questions and issues with respect to the new EO, and advise clients on compliance with the EO, and on how to permissibly avoid the imposition of sanctions.

For more information or questions regarding the subjects covered in this *Economic Sanctions Update*, please contact:

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The Eren Law Firm is an economic sanctions boutique. Its other core areas of concentration and practice include corporate transactions, and international dispute resolution, anti-money laundering, and international trade regulation. The Firm's clients from around the world include banks and financial institutions; insurance, reinsurance and other financial services companies; natural resource extraction companies, industrial companies, marine and air transportation companies, shipowners; sovereign governments; foreign state enterprises; and individuals.

Mr. Eren and Mr. Pinter of the Firm served at the U.S. Treasury's Office of Foreign Assets Control (OFAC), the U.S. government agency that administers and enforces U.S. economic sanctions, for a combined 25 years prior to entering private law practice, respectively 11 and 10 years ago, and they have devoted and continue to devote most of their time in private practice to economic sanctions issues and matters. Ms. Maucher of the firm advises on EU sanctions issues and matters.

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