

# CLIENT UPDATE

## FURTHER EXPANSION OF U.S. SANCTIONS AGAINST IRAN

### WASHINGTON, D.C.

Satish M. Kini  
smkini@debevoise.com

Liz Alspecter  
lalspector@debevoise.com

### NEW YORK

Carl Micarelli  
cmicarelli@debevoise.com

Eric P. Alpert  
epalpert@debevoise.com

Samuel E. Proctor  
seproctor@debevoise.com

On January 2, 2013, President Obama signed into law the “Iran Freedom and Counter-Proliferation Act of 2012” (the “IFCPA”) as part of the fiscal year 2013 National Defense Authorization Act.<sup>1</sup> The IFCPA represents the fourth time in three years that the U.S. Congress has passed legislation imposing new sanctions against Iran and comes merely six months after the last significant expansion of U.S. sanctions against Iran – the Iran Threat Reduction and Syria Human Rights Act (“ITRSHRA”).<sup>2</sup> The IFCPA targets Iran’s energy, shipping, shipbuilding and precious metals sectors and, like ITRSHRA, applies extra-territorially to companies operating outside the United States.

Beyond the legislative front, the U.S. Treasury Department’s Office of Foreign Assets Control (“OFAC”) continues actively to implement new Iran sanctions and to warn firms of Iran’s efforts to circumvent international sanctions. In particular, on January 10, 2013, OFAC issued an advisory on Iran’s use of exchange houses and trading

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<sup>1</sup> The Iran Freedom and Counter-Proliferation Act of 2012, Pub. L. 112-239, Title XII, Subtitle D (2013).

<sup>2</sup> We previously profiled ITRSHRA and its implications, *see* Debevoise & Plimpton Financial Institutions Report, Expansion of U.S. Sanctions Against Iran and Syria (Oct. 2012), and recently discussed the new reporting obligations arising out of ITRSHRA. *See* Client Update, SEC Reporting Companies Must Disclose Certain Iran-Related Activities (Jan. 15, 2013).

companies to evade U.S. sanctions (the “Advisory”) and recommends enhanced due diligence as a result.<sup>3</sup> Each of these developments is discussed below.

## THE IFCPA

As noted, the IFCPA expands U.S. sanctions against Iran and targets certain of its industries and sectors. Since U.S. entities (and, under ITRSHRA, entities owned or controlled by U.S. persons) are already prohibited from doing business with Iran, the chief aim of the new law is to restrict *non-U.S. persons* from doing business with Iran, even if such business may be permissible under those persons’ home-country legal regimes. A brief summary of IFCPA’s provisions, which are complex, is set forth below.

### *Energy, Shipping and Shipbuilding*

The IFCPA requires the President to block and prohibit all transactions in property, and interests in property, held by any person the President determines:

- Is part of the energy, shipping or shipbuilding sectors of Iran;
- Operates a port in Iran; or
- Knowingly provides significant support (including financial, material, technological or other support) to any person falling into the above two categories, or to any Iranian persons on OFAC’s Specially Designated Nationals and Blocked Persons List (“SDNs”).<sup>4</sup>

The IFCPA specifically identifies the National Iranian Oil Company (“NIOC”), the National Iranian Tanker Company (“NITC”) and the Islamic Republic of Iran Shipping Lines as “entities of proliferation concern” covered by the blocking provisions. The specific identification of these entities is consistent with ITRSHRA, which requires the U.S. Treasury Secretary to determine whether NIOC or NITC is an agent or affiliate of Iran’s Revolutionary Guards Corps and, therefore, subject to additional sanctions.<sup>5</sup>

In addition, the IFCPA generally requires the President to impose certain sanctions on any person that knowingly sells, supplies or transfers to or from Iran significant goods or services used in connection with the energy, shipping or shipbuilding sectors of Iran. There are certain limits and exceptions to this Presidential authority. First, the provision of

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<sup>3</sup> The Use of Exchange Houses and Trading Companies to Evade U.S. Economic Sanctions Against Iran (Jan. 10, 2013).

<sup>4</sup> IFCPA § 1244(c).

<sup>5</sup> The Secretary determined that NIOC (but not NITC) is an agent or affiliate of the Revolutionary Guards. See Press Release, U.S. Dep’t of the Treasury, Treasury Submits Report To Congress On NIOC And NITC (Sept. 24, 2012).

certain types of humanitarian, food and medical assistance does not trigger sanctions. Second, sanctions can be applied to exports of Iranian petroleum or petroleum products to particular countries only if the President determines that there is sufficient supply of non-Iranian petroleum in world markets.

The IFCPA also prohibits the opening of, and requires the prohibition or imposition of “strict conditions” on the maintaining of, a correspondent or payable-through account held by a U.S. financial institution on behalf of a foreign financial institution that has knowingly conducted or facilitated significant financial transactions in such goods or services with Iran.

### *Sale, Supply or Transfer of Precious Metals and Certain Other Materials*

The IFCPA requires the President to impose certain sanctions on persons who knowingly sell, supply or transfer, directly or indirectly, the following goods to or from Iran:

- Precious metals; and
- Graphite, raw or semi-finished metals (such as aluminum and steel), coal and software for integrated industrial processes if:
  - Iran is using the materials for any exchange or transaction, or listing any such materials as assets of the Government of Iran for purposes of its national balance sheet; or
  - The material is (i) to be used in connection with the energy, shipping or shipbuilding sectors of Iran or any sector of the economy of Iran determined to be controlled directly or indirectly by Iran’s Revolutionary Guard Corps; (ii) sold, supplied or transferred to or from an Iranian SDN; or (iii) to be used in connection with the nuclear, military or ballistic missile programs of Iran, as determined by the President.<sup>6</sup>

Foreign financial institutions that knowingly conduct or facilitate a significant financial transaction for the sale, supply or transfer of the above materials also are subject to sanctions.<sup>7</sup> The sanctions include a prohibition on the opening of, and the prohibition or imposition of “strict conditions” on the maintaining of, a correspondent or payable-through account by the foreign financial institution in the United States.<sup>8</sup>

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<sup>6</sup> IFCPA § 1245.

<sup>7</sup> IFCPA § 1245(c).

<sup>8</sup> IFCPA § 1245(c).

Importantly, the IFCPA provides an exception for persons who exercise due diligence to avoid these prohibitions. Specifically, the President may not impose sanctions where a person has exercised due diligence (in the form of policies, procedures and controls) to ensure that the person does not engage in the prohibited sale, supply, transfer or financing transactions.<sup>9</sup> The statute does not specify further what level of diligence will suffice.

### *Underwriting, Insurance and Reinsurance*

The IFCPA mandates that the President impose sanctions on persons that knowingly provide underwriting, insurance or reinsurance services:

- For any Iran-related activity for which sanctions have been imposed under U.S. law;
- To or for any person with respect to, or for the benefit of, any activity that is sanctioned under the IFCPA; or
- To or for any Iranian SDN, with some exceptions.<sup>10</sup>

As above, there is an exception for persons who exercise due diligence in establishing and enforcing official policies, procedures and controls to ensure that the person does not underwrite or enter into a contract to provide insurance or reinsurance for proscribed activities.<sup>11</sup>

### *Foreign Financial Institutions that Facilitate Transactions on Behalf of SDNs*

The IFCPA generally requires the President to prohibit the opening, and prohibit or impose “strict conditions” on the maintaining, of U.S. correspondent or payable-through accounts by foreign financial institutions that knowingly facilitate significant financial transactions on behalf of Iranian SDNs, with some exceptions.<sup>12</sup>

### *Additional Provisions*

The IFCPA contains a number of additional provisions. Among them are the imposition of sanctions on the Islamic Republic of Iran Broadcasting and its president,<sup>13</sup> which are

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<sup>9</sup> IFCPA § 1245(f).

<sup>10</sup> IFCPA § 1246(a)(1).

<sup>11</sup> IFCPA § 1246(d).

<sup>12</sup> IFCPA § 1247(a).

<sup>13</sup> IFCPA § 1248.

included on the SDN list, and on persons who misappropriate or divert goods, services, food and medicines intended for the people of Iran.<sup>14</sup>

## **OFAC ADVISORY**

OFAC's Advisory notes that, because of the stringent sanctions imposed against its financial system, Iran increasingly is relying on third-country exchange houses and trading companies to evade U.S. and international sanctions regimes. The Advisory is intended to alert U.S. financial institutions to these practices and to suggest enhanced due diligence in response.

### *Funds Transfer Practices that Evade Sanctions*

The Advisory identifies a number of funds transfer practices as potentially indicating an evasion of the Iran sanctions regime and gives examples of evasive transactions that U.S. financial institutions might encounter:

- An exchange house or trading company attempts to send a payment through the United States on behalf of a company domiciled in Iran and, after the payment is stopped for review, re-sends the payment with an altered address reflecting a non-sanctioned jurisdiction;
- An exchange house or trading company repeatedly attempts to send payments through the United States in violation of the Iran sanctions regime or otherwise repeatedly conceals or obscures Iranian involvement in payments routed through the United States; and
- The volume or frequency of payments involving an exchange house or trading company is inconsistent with the volume and frequency of payments that it generally conducts.

### *Enhanced Due Diligence*

The Advisory "suggests enhanced due diligence" on the part of U.S. financial institutions to mitigate the risk of processing these transactions. Specifically, the Advisory recommends:

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<sup>14</sup> IFCPA § 1249.

- Monitoring payments involving third-country exchange houses or trading companies that may be processing Iran-related transactions, and requesting additional information from them;
- Conducting account and transaction reviews of individual exchange houses or trading companies that repeatedly violate (or attempt to violate) the Iran sanctions regime; and
- Contacting and requesting additional information from correspondents that maintain accounts for, or facilitate transactions on behalf of, third-country exchange houses or trading companies that engage in Iran-related transactions.

U.S. financial institutions are well advised to incorporate OFAC's due diligence recommendations into their compliance regimes.

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In sum, the IFCPA and the Advisory represent additional steps in the United States' continuing efforts to isolate Iran from the global financial markets and business community. Both present new compliance obligations and challenges for firms that do business across borders and increase the risk of U.S. penalties from engaging in business activity, directly or indirectly, with Iran.

Please do not hesitate to contact us with any questions.

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