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**CLIENT ALERT:
THE U.S. RATCHETS UP SANCTIONS ON IRAN WITH BACK-TO-BACK ISSUANCE
OF PRESIDENT OBAMA'S EXECUTIVE ORDER AUTHORIZING "ADDITIONAL
SANCTIONS WITH RESPECT TO IRAN" AND PASSAGE OF THE "IRAN THREAT
REDUCTION AND SYRIA HUMAN RIGHTS ACT OF 2012"**

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INTRODUCTION

The United States continues to exert maximum economic pressure on Iran as evidenced by the recent issuance of President Obama's executive order on July 31, 2012 authorizing "Additional Sanctions With Respect To Iran" and passage of the "Iran Threat Reduction and Syria Human Rights Act of 2012," which has been pressed by Congress and awaits the President's signature. These measures collectively represent the most severe and broadest sanctions adopted to date by the U.S. against Iran, and have the potential to have significant repercussions in the financial, insurance and shipping industries. We set forth below our general overview of both the Executive Order and the new Act, as well as our thoughts and observations regarding the potential impact of

July 31, 2012.¹ are aimed at foreign financial institutions and foreign persons, and thus, have potential ramifications for those engaged in transactions having a connection to Iran's petroleum and petrochemical industries. A brief summary of the key provisions follows.

Sanctions Authorized Against "Foreign Financial Institutions"

Section 1 of the E.O. authorizes the Secretary of the Treasury, in consultation with the Secretary of State, to impose financial sanctions on "foreign financial institutions." Such institutions are defined in the E.O. to include a variety type of banking institutions, but notably "insurance companies" are not included within the entities described. Thus, it appears that this aspect of the E.O. is aimed primarily at foreign banks that engage in the sanctionable conduct described in Section 1. "Foreign financial institutions" can be sanctioned if they are found to have "knowingly conducted or facilitated any significant financial transaction" with the National Iranian Oil Company ("NIOC"), Naftiran Intertade Company ("NICO"), and/or any entities

**EXECUTIVE ORDER – JULY 31, 2012
("ADDITIONAL SANCTIONS WITH
RESPECT TO IRAN")**

GENERAL OVERVIEW

The new sanctions announced via Preident Obama's Executive Order of

¹ This Executive Order supplements a number of sanctions programs that have been enacted in the U.S. in recent years, including the Comprehensive Comprehensive Iran Sanctions, Accountability & Divestment Act of 2010 ("CISADA") and Executive Orders 13590 and 13608, amongst others.

owned or controlled by, or operating for or on behalf of NIOC or NICO.² Additionally, such institutions can be sanctioned if they knowingly conduct or facilitate significant financial transactions for the purchase or acquisition of petroleum, or petroleum or petrochemical products, *from* Iran through any channel (not just through NIOC or NICO).

According to the Office of Foreign Assets Control (the agency responsible for implementing sanctions within the Treasury Department),³ this provision is aimed at deterring Iran or any other country or institution from establishing workaround payment mechanisms for the purchase of Iranian oil to circumvent the oil sanctions authorized under the National Defense Authorization Act (NDDA).⁴ A “foreign financial institution” found to have engaged in any of the sanctionable activities can effectively be excluded from the U.S. financial system, by having its correspondent or payable-through accounts prohibited or restricted by the Treasury Department.

² The E.O. exempts from this section sales of refined petroleum products to NIOC or NICO that are below the dollar threshold that could trigger sanctions under the Iran Sanctions Act, Public Law 104-172, 50 U.S.C. §§1701, *et. seq.*

³ See <http://www.treasury.gov/resource-center/faqs/Sanctions/Pages/answer.aspx#216>.

⁴ The NDDA was signed into law on December 31, 2011. It contains petroleum-related sanctions applicable to both private and state-owned foreign financial institutions. The NDDA, however, permits waiver of its sanctions against foreign financial institutions if their home countries reduce their petroleum imports from Iran. Twenty such waivers have been granted, including to Japan, India, Singapore and China. Waivers remain in effect for 180 days and may be renewed for subsequent 180-day periods or withdrawn if countries increase their imports of Iranian oil.

Notably, (similar to the NDDA), sanctions can be imposed under §1 only if the President determines that there is a sufficient supply of petroleum and petroleum products in the world market (apart from Iran) to permit a significant reduction in the volume of products purchased from Iran.⁵ In this way, the E.O. seeks to balance the desire to reduce Iran’s petroleum revenues with the desire to maintain price stability in the global market.

Sanctions Authorized Against Any Person for Transactions with NIOC or NICO

Section 5 of the E.O. authorizes the Secretary of the Treasury, in consultation with the Secretary of State, to impose sanctions on any person (defined to include an individual or entity) who materially assists, sponsors or provides financial, material, or technological support for, or goods or services in support of, NIOC, NICO, or the Central Bank of Iran, and/or the purchase or acquisition (regardless of the channel) of U.S. bank notes or precious metals by the Government of Iran.

This aspect of the E.O. is not limited to U.S. persons, and as such, renders sanctionable the conduct of foreign persons who engage in the specified activity. The Secretary of the Treasury, in turn, is authorized to block the property within the U.S. of any person found to have engaged in the sanctionable conduct. This would include the ability to block the transfer of U.S. dollar transactions through the U.S. correspondent banking system. Consequently, by way of example, a foreign entity that “materially” provides goods or services to NIOC or NICO may

⁵ President Obama made such a determination on March 30, 2012 and again on June 11, 2012.

find its U.S. dollar transfers blocked by OFAC, even if that transfer is not a direct dealing with NIOC or NICO.

Sanctions Authorized Against Any Person for Petroleum-Related Transactions.

Perhaps the most material aspect of these new sanctions for foreign persons is contained in §2. Section 2 conveys primary sanction authority on the Department of State and authorizes it, in consultation with the Department of Treasury and other agencies, to impose sanctions on any person (not just U.S. persons) who knowingly engages in a “significant transaction for the purchase or acquisition” from Iran of petroleum or petroleum or petrochemical products.

Sanctions are also authorized against the successor of a person who engaged in such activities; those who own or control a person who engaged in the specified activity, and had knowledge that person engaged in those activities; and those who are owned or controlled by, or under common ownership or control with, such a person, and knowingly participated in the sanctionable activities. In this way, the E.O. seeks to target not only the person who engaged in the sanctionable conduct but also its subsidiaries and affiliates if they knew about or participated in the sanctionable activity.

Notably, as with the §1 sanctions, before sanctions can be imposed under §2, there must be a determination by the President that there is sufficient world market supply such that a significant reduction in the volume of purchased Iranian products is permissible.

IMPORTANT POINTS TO CONSIDER

There are several aspects of this new E.O. that warrant careful consideration by foreign persons who engage in transactions involving Iranian petroleum and petrochemical products.

- First, “significant transaction” is not defined, and thus it is unclear exactly what will constitute a “significant” transaction for purposes of triggering sanctions under the E.O. The Treasury Department has indicated that a number of factors are considered in determining “significance,” including size, number, and frequency; type, complexity, and commercial purpose; and the ultimate economic benefit conferred on the sanctions target. However, as explained, the State Department (not Treasury) will be primarily responsible for enforcing the §2 sanctions. While likely, it is not known definitively if the State Department will apply the same factors in assessing whether a transaction is significant.⁶
- Second, it is not entirely clear what type of transactions fall within the

⁶ As the State Department will enforce this aspect of the E.O., regulations are not likely to be enacted providing further clarification on the meaning and scope of the Section 2 sanctions program. Compare E.O. §12 authorizing the Treasury Department to promulgate regulations to carry out the purposes of certain sections and not mentioning §2. Such clarification will instead most likely come from a review of the actions actually taken by the State Department as it implements this program. In this way, this sanctions program is similar to the enforcement of CISADA under which the State Department has recently issued sanctions against foreign entities.

scope of the sanctionable activities. A plain reading of the E.O. suggests that it is aimed at preventing or limiting only the underlying sales transactions but not necessarily transactions incidental to the sale, i.e. such as transportation or insurance. Nonetheless, given the E.O.'s purpose, the State Department could attempt a broad construction of the provision so as to encompass services such as transportation or insurance which, although incidental, are necessary to effect the underlying sale. One could argue that such a construction would be inappropriate, particularly as other Iranian sanctions programs have expressly referred to insurance and shipping services,⁷ making the absence of such references indicative of an intent not to include same within this program.

- Individuals or entities determined to have engaged in sanctionable conduct will be subject to the same sanctions that may be imposed under the ISA. These include prohibiting transfers of payments through U.S. financial institutions to, from or on behalf of sanctioned persons, and the blocking of any such transfers. As such, a person found to have engaged in sanctionable conduct can find its ability to effect transactions in U.S. dollars prohibited and/or its U.S. dollar transactions stopped and held in the U.S.

⁷ Compare CISADA §102(a)(1) referring to “underwriting or entering into a contract to provide insurance ...” and “providing ships or shipping services to deliver refined petroleum products to Iran”.

“IRAN THREAT REDUCTION AND SYRIA HUMAN RIGHTS ACT OF 2012.”

GENERAL OVERVIEW

The purpose of this Act is to further curtail Iran’s ability to generate revenue from petroleum sales by both strengthening the enforcement of existing sanctions against Iran as well expanding the Iranian Sanctions Act of 1996 in key areas, including energy, insurance, financial and shipping related services. Specifically, of particular relevance to the shipping industry, the new sanctions targets any person that owns, operates, or insures a vessel that knew or should have known that the vessel was used to transport crude oil from Iran to another country. Likewise, the sanctions also target owners whose vessels ship Iranian petroleum products in a manner that attempts to conceal the Iranian origin of the products. The Act also contains specific provisions targeting the National Iranian Oil Company and the National Iranian Tanker Company and permits the President to apply sanctions against any person that provides underwriting services or insurance for either of these two companies.

SPECIFIC PROVISIONS OF THE ACT BEARING UPON THE SHIPPING AND INSURANCE INDUSTRIES

A summary of some of the more significant provisions relevant to the shipping and insurance industries are as follows:

Sec. 201 – Expansion of Sanctions with Respect to Iran’s Energy Sector

This section provides for exceptionally wide reaching sanctions touching on virtually any activity – including all “goods, services, technology or support”

– “that could directly and significantly contribute to the maintenance or enhancement” of Iran’s ability to develop petroleum resources or the domestic production of refined petroleum or petrochemical products. These sanctions extend to the provision of “any direct and significant assistance with respect to the construction, modernization, or repair of petroleum refineries or directly associated infrastructure, including construction of port facilities, railways, and roads, the primary use of which is to support the delivery of refined petroleum products.”

Sec. 202 – Imposition of Sanctions for Transportation of Crude Oil from Iran and Evasion of Sanctions by Shipping Companies

This section provides for imposition of sanctions on a person that owns, operates, controls or insures a vessel used to transport crude oil from Iran to another country. This section also provides for sanctions on a person that owns, operates or controls a vessel in a manner that conceals the Iranian origin of crude oil or refined petroleum products, such as by suspending the vessel’s satellite tracking device or obscuring or concealing the ownership, operation or control of the vessel by the Government of Iran or the National Iranian Tanker Co. or the Islamic Republic of Iran Shipping Lines. Vessels involved in these violations may be barred from calling at U.S. ports for a period of up to two (2) years. With respect to sanctions arising from the provision of underwriting, insurance or reinsurance for vessels operating in violation of this section, i.e. carrying crude oil from Iran or concealing the origin of Iranian crude oil or refined petroleum products, the Act provides an exception where it can be shown that the person providing such services had exercised “due diligence” in establishing

and enforcing policies, procedures and controls to ensure that the person does not provide such services for the transportation of crude oil or refined petroleum products from Iran in violation of this section. (In passing, it is interesting to note that while the subsection that addresses the concealment of Iranian origin of crude and refined products does not specifically reference underwriting/insurance services, this exception is nevertheless made applicable to that subsection. Thus, there appears to be somewhat of an inconsistency in the terms of this section of the Act.)

Section 203 – Expansion of Sanctions With Respect to Development by Iran of Weapons of Mass Destruction

This section allows the President to impose sanctions against any person that “exported or transferred, or permitted or otherwise facilitated the transshipment of, any goods, services, technology, or other items” which would “contribute materially” to Iran’s ability to “acquire or develop” chemical, biological or nuclear weapons, or “related technologies,” or “destabilizing numbers and types of conventional weapons.” This section also provides for sanctions in connection with any person that engages in a joint venture with Iran, or an entity incorporated in Iran or acting on behalf of or at the direction of Iran, relating to the mining, production or transportation of uranium.

Section 211 – Imposition of Sanctions With Respect to the Provision of Vessels or Shipping Services to Transport Certain Goods Related to Proliferation or Terrorism Activities to Iran

This section provides sanctions as to any person who “knowingly sells, leases or provides a vessel or provides 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 acts of international terrorism....” Under the Act, any “person” includes not only the person who sold, leased, or provided a vessel or provided insurance or other shipping services, but also includes any person that is a successor entity of such person or owns or controls such person. It is significant to note that the Act does not offer guidance on what goods may “materially contribute” to the Government of Iran in creating weapons of mass destruction.

Section 212 – Imposition of Sanctions with Respect to Provision of Underwriting Services or Insurance or Reinsurance for the National Iranian Oil Company or the National Iranian Tanker Company

This section provides for sanctions to be imposed on a person who “knowingly...provides underwriting services, or insurance or reinsurance for the National Iranian Oil Company, the National Iranian Tanker Company, or a successor entity to either such company.” The provision allows for an exception where the person providing such services had exercised “due diligence” in establishing and enforcing policies, procedures and controls to ensure that the person does not provide such underwriting services, etc. to the named companies.

CONCLUSION

The sanction regime set forth in the Executive Order of July 31, 2012, coupled with the recent enactment of the Iran Threat Reduction and Syria Human Rights Act of 2012, represents an exceptionally broad and concerted effort to severely curtail, if not eliminate, Iran’s ability to generate revenue from its petroleum resources. It is evident that many of these provisions have a direct and unequivocal impact on the maritime shipping and insurance industries. In other instances, the effect on shipping and insurance may be less obvious and will ultimately rest on just how broadly the U.S. Government interprets and enforces the particular sanction. Nevertheless, in either case, those in the shipping and insurance industries will clearly have to be mindful of these expanded sanctions and adjust accordingly to this new - and still evolving - environment.

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