

CISADA and the expansion of U.S. sanctions against Iran



The Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ('CISADA') broadens the scope of sanctions that can be imposed on those engaged in business activity with Iran. Jason M. Waite and Diego S. Marquez consider its impact.

On 1 July 2010, President Obama signed the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ('CISADA') into law. This expansion of U.S. sanctions, and the sanctions imposed by the United Nations and the European Union in the Summer of 2010, and by Japan and South Korea in September 2010, suggested a growing global consensus on the need for the international community to further isolate the Iranian regime.

One year later, as this article goes to press, news of an alleged Iranian plot to assassinate the Saudi ambassador to the United States in a Washington restaurant has heightened concerns in the U.S. capital about the Iranian regime and CISADA has come under review in the United States Congress as the government considers further actions.

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This article summarizes the changes enacted through CISADA to expand the scope of sanctions that may be imposed against companies engaged in

certain activities, the steps that the Obama administration has taken to implement the new sanctions over the last year, and how the expanded sanctions have impacted the worldwide business community. The article then offers recommendations for companies interested in maintaining compliance to avoid the imposition of the expanded sanctions, and concludes by considering the types of additional actions that could be taken by the United States.

CISADA: expanding the scope of existing sanctions

CISADA amends the Iran Sanctions Act ('ISA') to broaden the scope of sanctions targeting investments in Iran's energy sector. In particular, CISADA expands the activities subject to sanctions and establishes additional sanctions that can be imposed on those engaged in such activities.

The ISA authorized sanctions on any person that (1) invested more than \$20m in the enhancement of Iran's ability to develop petroleum resources or (2) exported, transferred or otherwise provided to Iran goods, services, technology or other items knowing that the provision of such items would contribute materially to Iran's ability to develop or acquire weapons of mass destruction or certain other advanced weapons. The new sanctions under CISADA similarly target investments (\$20m or more or \$5m per investment, totaling \$20m or more in a 12-month period) that directly and significantly contribute to the enhancement of Iran's ability to develop its petroleum resources. However, CISADA goes further than the ISA in terms of its scope of prohibited activity and provides for new 'triggers' that would require the imposition of sanctions.

Specifically, CISADA provides that the President must impose sanctions against a person he determines 'knowingly' sells, leases or provides any of the following, when such items have a fair market value of \$1m or more or an aggregate fair market value of \$5m or more in a 12-month period:

- goods, services or technology that could directly and significantly facilitate the maintenance or expansion of Iran's domestic production of refined petroleum products;
- refined petroleum products (to Iran); or
- goods, services or technology that could directly and significantly contribute to the enhancement of Iran's ability to import refined petroleum products.

While the law requires persons to act 'knowingly', that term is defined to include both actual knowledge and constructive knowledge.

Congress identified the refined petroleum industry as a vulnerability of the Iranian regime; at the time of CISADA's passage into law, Congress estimated that Iran imported between 25% and 40% of its refined oil needs due to limited domestic refining capacity. Believing that refined-petroleum-related sanctions could have a significant impact on the Iranian economy, Congress targeted more than the mere sale or provision of refined petroleum products or significant investments in the Iranian oil industry. The 'triggers' for the imposition of sanctions extend to a wide range of activities that could enhance Iran's refining capacity or assist in the delivery of refined petroleum products. The triggers now include assistance in the construction,

modernization or repair of petroleum refineries, including through the sale of parts and equipment, or the transfer of technology, as well as less direct contributions to Iran's refined petroleum industry, such as certain insurance or reinsurance services, financing or brokering services, the supply of ships and the provision of shipping services.

Prior to CISADA, the President had available to him a menu of six options from which to choose sanctions once a determination was made that an entity was violating the ISA. Now, under the ISA as amended by CISADA, the President has three new options available on the menu of sanctions, options that specifically target access to financial services by allowing the President to prohibit foreign exchange transactions and banking transactions, and broad authority to block property subject to U.S. jurisdiction. The chart 'Available sanctions' lists the sanctions that may be imposed by parties found to be engaged in prohibited conduct.

The newly available sanctions are significant in their scope; the prohibition on transactions with respect to property subject to U.S. jurisdiction, for example, essentially means that an entity subject to this sanction is prevented from doing any business with U.S. persons even where that business takes place entirely outside the United States. The impact is likely to be felt by a sanctioned party even more broadly than is actually intended given the practice of many global companies to screen all of their worldwide transactions against lists of prohibited parties and their tendency to avoid business with such parties as a prophylactic matter, even if U.S. persons may not be involved in the transaction. Indeed, the three additional sanctions greatly expand the President's power to reach foreign entities doing business with Iran.

There are additional provisions of CISADA beyond those described above. These include provisions calling for the imposition of sanctions on foreign banks that knowingly facilitate Iranian efforts to acquire weapons of mass destruction or engage in doing business with key Iranian banks, the Iranian Revolutionary Guard Corps ('IRGC') or entities sanctioned by the UN Security Council. U.S. regulators have been active in implementing these requirements, including in a rule

Available sanctions

Sanctions available under the ISA

- Denial of Export-Import Bank loans, credits, or credit guarantees for U.S. exports
- Denial of licences for the export of military, dual-use, or nuclear-related goods or technology
- Denial of U.S. bank loans exceeding \$10m in any 12-month period
- Prohibition on service as a primary dealer in U.S. government bonds, and/or prohibition on serving as a repository for U.S. government funds, if the sanctioned party is a financial institution (each counts as one sanction)
- Prohibition on U.S. government procurement from the sanctioned party
- Restriction on imports from the sanctioned entity

Sanctions now available under CISADA

- Prohibition on foreign exchange transactions subject to U.S. jurisdiction
- Prohibitions on banking transactions subject to U.S. jurisdiction
- Prohibitions on transactions with respect to any property subject to U.S. jurisdiction in which the sanctioned party has an interest

promulgated by the Treasury Department's Financial Crimes Enforcement Network ('FinCEN;'), effective 11 October 2011, that requires U.S. banks, upon request from FinCEN, to inquire of certain foreign banks for which the U.S. bank maintains a corresponding account as to the activities of those banks with respect to certain parties of concern. Administration officials have indicated that FinCEN has already issued requests to certain foreign banks suspected of dealings with designated entities.

CISADA also includes provisions targeting officials responsible for human rights abuses, exporters of technology used to restrict communications, and countries that allow for diversion of certain goods, technologies and services. It imposes new requirements on U.S. government contractors and grants state and local governments the authority to adopt and enforce measures to divest government funds from entities engaging in business with Iran's energy sector. Indeed, many state pension funds have begun reviewing the activities of companies in which they are invested and divesting from those engaged in Iran business, and certain states, including California and Florida, have implemented state laws prohibiting state government contracts with companies investing in Iran's energy sector (see, *WorldECR* issue 4).

Mandatory investigations and the enforcement of CISADA

Critics of the sanctions in place prior to CISADA questioned the level of discretion left to the President in determining whether to investigate activities that could trigger sanctions. The ISA stated that the President 'should' investigate potentially sanctionable activity, but the ISA did not require an investigation. CISADA represents a significant change in that it amends the ISA to require that the President investigate activities that could potentially violate the act's prohibitions.

President Obama delegated his authority to investigate potential violations of the ISA as amended by CISADA to the Department of State in a presidential memorandum dated 23 September 2010 (through which the President also delegated other authority under CISADA to both the departments of State and Treasury). Investigations are being handled by the Office of Terrorism Finance and Economic Sanctions Policy ('OTFESP'). Some members of Congress have lamented the lack of resources in the OTFESP and delays in the investigation process. Others have expressed frustration over the office's apparent failure to initiate investigations into certain companies publicly suspected of having engaged in sanctionable activities.

However, the administration has taken a number of actions to enforce

CISADA. On 30 September 2010, the State Department announced that Naftiran Intertrade Company, a Swiss company owned by National Iranian Oil Company, would be the first entity sanctioned under CISADA. The State Department then sanctioned Belarusneft, a state-owned Belarusian energy company, in March 2011 for having entered into a \$500m contract with Naftiran to develop an oilfield in

Iran. On 24 May 2011, the State Department announced sanctions against seven companies under CISADA: PCCI, Royal Oyster Group, Speedy Ship, Tanker Pacific, Ofer Brothers Group (later clarified to list specific members of the group), Associated Shipbroking, and Petroleos de Venezuela ('PDVSA') for shipping transactions involving refined petroleum products. These May 2011

sanctions represent a significant development given that they targeted companies providing shipping services and not just companies investing directly in Iran's energy sector, providing an example of the extended reach of sanctions under the ISA as amended by CISADA.

The administration has also used its authority under CISADA to persuade companies to wind down business with

Impact on business – new compliance considerations

As we wait to see whether the Obama administration will take further actions under CISADA, companies should evaluate their own compliance and susceptibility to CISADA sanctions. Because the sanction 'triggers' under CISADA now include assistance in the construction, modernization or repair of petroleum refineries as well as less direct contributions to Iran's refined petroleum industry (such as the supply of equipment and technology, insurance or reinsurance services, financing or brokering services, and the supply of ships and shipping services), the sanctions could impact companies and industries one or two steps removed from the energy sector. For example, transportation and shipping companies, logistics providers, industrial equipment and machinery producers, infrastructure development companies, consultants and other service providers should examine their customer base, analyze the potential uses of their goods, services, or technologies, and consider the potential impact of the CISADA sanctions on their business. Given the reach of the sanctions available to the President under CISADA, even companies with no U.S. business should take proactive measures to ensure their activities are not sanctionable.

Companies can take various steps to avoid engaging in sanctionable activities under CISADA. Generally speaking, this calls for increased due diligence in undertaking new business. Entities operating in the energy sector or providing construction, maintenance or other services to that sector should weigh the full scope of their activities against the list of activities that could trigger

sanctions. Companies outside the energy sector should also analyze the extent to which supply of their products or services, even general use goods, such as pipes, valves, pumps, power generation systems, and other significant machinery and equipment, could potentially trigger sanctions. Logistics companies, insurance and other financial services providers, for example, should take active steps to understand their customers' business. It is often difficult for such companies to know the types of goods or services that could serve to enhance Iran's petroleum refineries or Iran's ability to import refined petroleum, but through active efforts to know their customers, such companies can reduce the risk of engaging in activities that could be considered to be sanctionable.

Implementing clear written internal policies and procedures can also help mitigate risk. CISADA provides that no sanctions are to be imposed on underwriters, insurers, or reinsurers that exercise due diligence in establishing and enforcing official policies, procedures and controls that aim to ensure compliance with the prohibition on support to Iranian imports of refined petroleum products. This exception suggests that, at minimum, companies, including those outside the insurance and re-insurance industries, would be wise to have such compliance controls in place. Companies should also consider adopting business practices that further protect against potential violations. The State Department, for example, encourages the use of coverage exclusions in insurance policies for losses associated with the delivery of refined petroleum products. Similarly, shipping associations have suggested

employing contractual language that allows ship owners to refuse to deliver refined petroleum cargoes to Iran. These types of contractual provisions help protect such service providers from the risk of engaging in sanctionable activity, and similar approaches can be developed for other sectors and types of business.

Lastly, after identifying activities that are or may be sanctionable under CISADA, companies should weigh the benefits of approaching the State Department, OTFESP, under the 'special rule' to clarify the permissibility of the activities, and, if necessary, negotiate a winding-down of any operations of concern and avoid the business and reputational costs of a State Department investigation and potential subsequent sanctions. It is generally understood that companies may be permitted to fulfil existing contractual obligations, but the detailed nature of such obligations will have to be presented to the U.S. government. Indeed, companies availing themselves of the special rule are encouraged to provide a detailed catalogue of their existing activity in Iran as well as their plan for winding down any sanctionable activity as soon as possible. Companies with U.S. affiliates, or even companies that merely employ U.S. persons or have U.S. board members, will need to be comfortable that these U.S. persons have not been engaged in activities related to Iran that would constitute violations of the generally applicable Iran sanctions administered by the Office of Foreign Assets Control ('OFAC'), and, if necessary, address potential OFAC regulatory concerns prior to or concurrent with any approach to the State Department.

Iran. In fact, several companies have avoided investigation by the Obama administration because of the 'special rule' in CISADA that allows the President to decline to investigate companies that agree to wind down prohibited activities and certify that they will no longer engage in such activities. On 30 September 2010, for example, the State Department announced that Royal Dutch Shell PLC of the Netherlands, Total SA of France, Statoil ASA of Norway and ENI SPA of Italy had all agreed to take advantage of the special rule and cease prohibited activities involving Iran. A fifth company, INPEX of Japan, similarly pledged to end its sanctionable activities in Iran in exchange for avoiding investigation.

Additionally, the State Department reports that several companies have voluntarily decided to stop business

companies have been targeted by the administration, other suspected violators have not been investigated. Members of Congress, for example, have identified potential violators and inquired about such entities with the President, yet it is unclear whether such companies have been investigated. Similarly, a letter co-signed by 92 U.S. senators was delivered to the administration in August 2011 urging the President to sanction the Central Bank of Iran ('CBI'), using CISADA or other authorities available to him. There is growing frustration in the Congress over the administration's lack of action with respect to the CBI.

Increased enforcement and additional sanctions likely

The pressure on the Obama administration is increasing with

Legislation has been introduced in the Senate that would define what constitutes 'credible information' requiring initiation of an investigation, and would explicitly require the President to take action with respect to entities potentially engaged in sanctionable activity and identified in written requests by members of Congress. Senator Robert Menendez (D-NJ) has proposed legislation that would prohibit EU refiners from using Iranian crude oil in gasoline exported to the United States, while senator Jon Tester (D-MO) has asked the administration to close a 'loophole' and consider enforcing the more general OFAC-administered IEEPA-based Iran sanctions against foreign subsidiaries of U.S. companies, though such a change would likely require legislation to amend IEEPA and such efforts have failed in the past. For its part, the administration is engaged in diplomatic efforts to persuade countries like China, Spain, Japan, South Korea, India and Turkey to limit business with Iran's energy sector.

While CISADA has had an impact on Iran's ability to develop its petroleum industry, the impact has done little to assuage concerns in the United States about Iran's efforts to develop a nuclear programme, its support for terrorist groups, and human rights abuses. Given the continuing pressure on the administration, further actions under CISADA against companies engaged in business related to Iran are expected, and additional development or expansion of the overall U.S. sanctions regime remains a distinct possibility.

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with Iran since implementation of CISADA, including Turkish refiner Tupras, Kuwait's Independent Petroleum Group, India's Reliance, Malaysia's Petronas, Russia's Lukoil and Swiss energy traders Vitol, Glencore, and Trafigura. Repsol, BP, South Korea's GS Engineering & Construction and the German firm Linde have abandoned ongoing development projects or promised to forego planned participation in future projects, and Germany's ThyssenKrupp has gone a step further and offered to freeze all new business with Iran, even business outside the energy sector. Major insurers, such as Lloyd's of London, have stopped covering shipments of refined petroleum to Iran. Hong Kong shipping company NYK Line Ltd. has decided to withdraw from all trade with Iran.

Despite this flurry of activity over the past year, pressure is increasing on the Obama administration to do more. It is not clear that the sanctions have significantly disrupted the Iranian regime's efforts to obtain nuclear weapons. Moreover, while certain

respect to Iran, and frustration with the Iranian regime is growing in Washington, particularly following the news of its alleged involvement in a plot to assassinate the Saudi Ambassador. The Senate Committee on Banking, Housing & Urban Affairs held a public hearing on 13 October 2011 to discuss implementation of the CISADA sanctions with Obama administration officials. The House Foreign Affairs Committee followed suit on 14 October. During testimony before both committees, David Cohen, the Under Secretary of the Treasury for Terrorism and Financial Intelligence, indicated that 'all options' remain on the table for increasing financial pressure on the Iranian regime, including the CBI sanctions requested by 92 senators. Members of Congress continue to press not only for sanctions against the CBI but for an increase in the number of investigations of foreign banks and companies, additional designations of Iranian human rights abusers, and further efforts to pressure the European Union and other allies to stop purchases of Iranian crude oil.

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