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## Sanctions Round-Up: First Quarter 2013

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**The first quarter of 2013 was marked by various efforts by the Treasury Department’s Office of Foreign Asset Control (“OFAC”) to provide some much-needed guidance and support to persons attempting to comply with ever more complicated US sanctions, including the launch of an updated online search tool. Meanwhile, previously existing exceptions to the Iranian sanctions regime narrowed even further, and OFAC continued to crack down on foreign sanctions evaders. OFAC and the State Department also renewed efforts to use sanctions to curb North Korea’s proliferation of weapons of mass destruction and to bolster counterterrorism efforts around the globe. Finally, US policies toward the Burmese regime and Syrian opposition forces continued to shift, with new licenses authorizing certain previously prohibited transfers of funds.**

### OFAC Releases New SDN Search Tool

On March 14, 2013, OFAC made publicly available a new version of its [online SDN Search Tool](#). This upgraded tool applies so-called “fuzzy logic” algorithms to account for possible differences in spelling or transliteration in searched names. The SDN Search tool now uses a scoring system that indicates the similarity between the name entered and the resulting matches on the SDN List. A score of 100 indicates an exact match, while lower scores

indicate potential matches. Users select a “match threshold” via slider bar to reflect how broad of a search they would like to conduct. A value of 100 will return only names that exactly match the characters entered into the name field. A value of 50 will return all names that are deemed to be 50% similar based upon the matching logic of the search tool. There is also a “minimum name score field” that permits users to limit the number of names returned by a search. Users can assess the quality of resulting matches by comparing the name entered with the name on the SDN list along with all additional information listed, which often includes nationality, passport, tax ID, former names, etc. The OFAC hotline can also be used to verify potential true matches.<sup>1</sup>

In its announcement releasing the new tool, OFAC specifically stated its intention to assist medium- to small-sized businesses and individuals who have fewer resources to spend on compliance efforts. However, OFAC declined to provide a recommendation as to the appropriate match threshold to use when conducting an SDN search. Instead, OFAC vaguely directs users to make their own determinations of the proper threshold based on “internal risk assessments” and “established compliance practices.”

### Additional Provisions Targeting Iran Go Into Effect

Sanctions provisions targeting Iran went into effect on February 6, 2013, which marked the passage of 180 days from President Obama’s signing of the Iran Threat Reduction and Syria Human Rights Act of 2012 (the “Threat Reduction Act” or “TRA”). That same day, OFAC published answers to frequently asked questions relating to the implementation of those provisions, including section 504 of the TRA.

Pursuant to section 1245(d)(4)(D) of the National Defense Authorization Act for Fiscal Year 2012 (“NDAA”) and the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (“CISADA”), foreign financial institutions face restrictions on access to, or even the complete loss of, their correspondent accounts in the United States if they knowingly engage in significant financial transactions with the Central Bank of Iran or any other designated Iranian financial institution relating to the purchase of petroleum or petroleum-related products from Iran, unless an exception applies. Most notably, the NDAA’s “significant reduction exception” applies to foreign financial institutions within those countries that the Secretary of State, in consultation with the Secretary of the Treasury and other agencies, has determined to have significantly reduced their purchases of Iranian crude oil. The exception, which has been granted to twenty countries to date, must be renewed every 180 days.<sup>2</sup> Countries that have reduced their Iranian crude oil purchases to zero may continue to receive the significant reduction exception.

As of February 6, 2013, section 504 of the TRA narrowed this significant reduction exception to apply only to transactions that facilitate bilateral trade between a country that has received an exception and Iran. The funds resulting from such bilateral trade must either be used to pay for a purchase by Iran of goods or services from the country sold directly to Iran or credited to a special purpose account within the country. Funds may not be repatriated to Iran or any third country.<sup>3</sup>

<sup>1</sup> The OFAC hotline can be reached at 1-800-540-6322.

<sup>2</sup> The countries that have received exceptions are Japan, China, India, Malaysia, South Korea, Singapore, South Africa, Sri Lanka, Taiwan, Turkey, Belgium, the Czech Republic, France, Germany, Greece, Italy, the Netherlands, Poland, Spain, and the United Kingdom. On March 13, 2013, the State Department extended for another 180 days the exceptions initially granted in March 2012 to Japan and the ten European Union countries. The remaining countries’ exceptions will be subject to renewal in June 2013.

<sup>3</sup> A “special purpose account” is an account set up in the name of the Central Bank of Iran or a non-designated Iranian financial institution that can only be used for bilateral trade or for sales of humanitarian goods. A special purpose account may not be used to make payments to the

Overall, this narrowing of the significant reduction exception effectively locks up Iranian oil revenue overseas and limits Iran's ability to move funds across jurisdictions. Section 504 also eliminates the previously existing distinction between state-owned or -controlled foreign financial institutions and private foreign financial institutions, expanding the scope of sanctionable transactions to include the former (foreign central banks still do not fall within the scope of the NDAA).

OFAC's guidance on section 504 of the TRA clarifies the types of transactions that now fall outside of the significant reduction exception. Bilateral trade does not include brokering transactions involving goods or services from or to third countries. For instance, if a foreign financial institution in a country that has received an exception facilitates a third country's crude oil purchase—even a third country with a significant reduction exception—from Iran, that foreign financial institution would have exposure to sanctions because the transaction was not solely for the institution's host country's purchase of crude oil from Iran. The guidance also notes that because the National Iranian Oil Company ("NIOC") was designated under Executive Order 13382 in November 2012, only transactions solely for the purchase of petroleum or petroleum products from NIOC will fall within the scope of the significant reduction exception. A foreign financial institution in a significantly reducing country that is found to knowingly facilitate other types of transactions with NIOC will face exposure to sanctions. The purchase or acquisition of petrochemicals from Iran remains a sanctionable activity and is not subject to the significant reduction exception.

OFAC published separate guidance on February 6, 2013 making clear that humanitarian trade, including the sale of agricultural commodities, food, medicine, or medical devices to Iran, is not impacted by section 504 or other Iranian sanctions. The guidance also details the specific procedures for license applications. General licenses already allow for the export or re-export by US persons of certain food items, medicines, and basic medical supplies to Iran without further specific authorization, subject to certain limitations. Financial transactions in support of trade in certain food, medicine, and medical devices from the US (or from a foreign country), may also be conducted without specific OFAC authorization, subject to certain restrictions. Further, US sanctions regulations permit US financial institutions to process noncommercial, personal remittances to Iran, so long as the payment is processed through a third-country financial institution before reaching Iran.

On March 15, 2013, OFAC amended Part 561 of the Code of Federal Regulations, which contains the Iranian Financial Sanctions Regulations ("IFSR"), to incorporate changes made by sections 503 and 504 of the TRA.<sup>4</sup> For example, a new section was added to define the terms "reduce significantly," "significantly reduced," and "significant reduction" to include section 504's clarification that countries that have reduced their Iranian crude oil purchases to zero may continue to receive the significant reduction exception. New paragraphs were also added to implement the narrower scope of the significant reduction exception, such as the inclusion of a definition of "bilateral trade" and a detailed description of the restrictions on what can be done with the funds resulting from such trade with Iran.

## OFAC Continues to Target Foreign Sanctions Evaders

During the first few months of 2013, OFAC proactively sought to stem the evasion of US sanctions targeting Iran by identifying some of the mechanisms used to circumvent sanctions. On January 10, 2013, OFAC issued advisory guidance

Government of Iran or any financial institution that appears on OFAC's "List of Foreign Financial Institutions Subject to Part 561" (providing the names of foreign financial institutions sanctioned under the NDAA and CISADA).

<sup>4</sup> The IFSR codify in part the sanctioning authority held by the US government and generally implicate foreign financial institutions and their access to the US financial system.

cautioning that Iran has begun to use third-country exchange houses and trading companies to process funds transfers through the United States on its behalf.<sup>5</sup> The OFAC advisory identifies the evasive practices used by such third-country entities, including the omission of references to Iranian addresses or names on payment messages. The guidance also highlights potential red flags, such as the fact that these third parties (i) often lack their own US correspondent accounts and instead rely on their banks' correspondent accounts to access the US financial system; (ii) are often located in jurisdictions that are considered high-risk from a sanctions perspective; and (iii) process primarily commercial transactions rather than personal remittances. Uncharacteristic spikes in activity or activity that is inconsistent with the type of business generally conducted by an entity are additional warning signs. The OFAC advisory notes that it is not suggesting that accounts with all exchange houses and trading companies be closed but rather encouraging US financial institutions to perform enhanced due diligence, such as requesting additional information from correspondent banks or performing account or transactions reviews, when appropriate.

Further, in mid-March, OFAC Director Adam Szubin warned that the use of institutional accounts at brokerages could be exploited by foreign sanctions evaders. The structure of such "omnibus accounts," made up of sub-accounts held by a brokerage on behalf of other clients, allows the beneficial owners of those accounts to shield their participation from regulators and financial institutions' screening efforts. Speaking at a conference of anti-money laundering specialists, Mr. Szubin further cautioned that the opaque areas of any business model are where many institutions found themselves most at risk for sanctions liability.

OFAC also imposed penalties on front or shell companies acting on behalf of Iran to evade US sanctions. For example, on March 14, 2013, OFAC imposed sanctions pursuant to E.O. 13599 on a Greek businessman alleged to have facilitated Iran's evasion of US sanctions on Iranian oil exports.<sup>6</sup> Dimitris Cambis, who owns the Greek shipping company Impire Shipping Ltd., purportedly used Iranian funds to purchase at least eight oil tankers and fill them with hundreds of millions of dollars' worth of Iranian oil that was subsequently sold to international customers unaware of the oil's origins. OFAC also imposed sanctions on the eight tankers purchased by Mr. Cambis; the eight purported "front companies" that nominally own those tankers; and a network of Iranian government front companies that provided the funds used to purchase the tankers. US persons are generally prohibited from engaging in any transactions with Mr. Cambis or the entities blocked pursuant to E.O. 13599, and any assets they may have under US jurisdiction are blocked. The State Department concurrently imposed a visa ban on Mr. Cambis and the corporate officers of the designated entities under the Iran Sanctions Act, as amended by the Threat Reduction Act.

Finally, in an announcement highlighting the gravity with which it will view attempts to circumvent US sanctions, an OFAC official stated in late March the agency's intention to start holding individuals personally responsible when their institutions help countries evade economic sanctions. Importantly, this means that individual bankers may now be subject to fines if there is evidence that they directed sanctions-evading activities, such as stripping information that could lead to the identification of a sanctioned party from a wire transfer payment message. To date, OFAC enforcement cases have typically resulted in extensive civil penalties at the corporate level. Although OFAC lacks the authority to bring

<sup>5</sup> Third-country exchange houses are financial institutions licensed to deal in foreign exchange and transmit funds on behalf of individuals and companies. Trading companies are entities that are not licensed to transmit funds, but in practice operate as exchange houses and rely upon their bank accounts to transmit funds on behalf of third parties.

<sup>6</sup> E.O. 13599 blocks the property of the Government of Iran or those acting on its behalf.

criminal actions against individuals, it may refer appropriate cases to the Department of Justice, thereby exposing individuals to additional penalties, including incarceration.

## Section 219 Disclosures Begin

Under section 219 of the Threat Reduction Act, US and foreign companies registered with the Securities and Exchange Commission (“SEC”), i.e., SEC-registered issuers, must disclose their dealings with Iran in their SEC filings effective February 6, 2013. When doing so, these issuers must detail their (and their affiliates) activities and contacts with Iran, including those of individual members such as board members and senior executives. Specifically, section 219 requires disclosure of any “transaction or dealing” by the issuer or its affiliates with: (i) the “Government of Iran” as defined by OFAC; (ii) persons or entities designated by OFAC for supporting global terrorism; or (iii) persons or entities designated by OFAC for supporting weapons of mass destruction proliferation activities. The filing of a disclosure under section 219 triggers a requirement for the SEC to submit a report to the President, who in turn is required to initiate an investigation into the possible imposition of sanctions and make a determination within 180 days with respect to whether sanctions should be imposed.

As of late March 2013, more than 100 SEC-registered reporting issuers had made disclosures regarding Iran or SDN-related activity. These disclosures make clear that there is a lack of guidance from US authorities as to how to properly comply with section 219, with some issuers even including affirmative statements as to the lack of any activity that needs to be disclosed. Across the board, reporting issuers have taken a very broad view of the meaning of “affiliate” and have recognized that there is no de minimus value threshold for reporting under Section 219, resulting in the disclosure of even extremely attenuated connections with Iran. Still, the apparent intent of Section 219 is being fulfilled as disclosed activities to date were primarily conducted by non-US affiliates. Issuers, where appropriate, have emphasized that the disclosed business activities are, in their view, compliant with US sanctions law or were compliant at the time of the activities. Of course, it remains to be seen whether the US authorities will agree with these assessments.

Shearman & Sterling’s full analysis of the disclosures that have been made to date is provided in the previously published client notes, [“Flash Report: Section 219 Disclosures Under the Iran Threat Reduction and Syria Human Rights Act of 2012.”](#) dated February 14, 2013, and [“What’s Going On—Over a Month of Section 219 Disclosures Under the Iran Threat Reduction and Syria Human Rights Act of 2012.”](#) dated March 20, 2013.

Additional guidance regarding the section 219 reporting requirement can be found in [“Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012—Additional Reporting Requirements for US Domestic and Foreign Issuers Registered with the SEC.”](#) dated November 8, 2012; [“SEC Publishes CD&Is for Iran Sanctions Disclosures Required Under Exchange Act Section 13\(r\).”](#) dated December 6, 2012; and [“The Iran Threat Reduction and Syria Human Rights Act of 2012—How Are You Planning to Comply with Section 219’s New Reporting Requirements?.”](#) dated December 17, 2012.

## Burma Sanctions Continue to Be Lifted

On February 22, 2013, OFAC issued General License No. 19, which authorizes US persons to conduct most transactions—including the opening and maintenance of correspondent accounts—with four of Burma’s major financial institutions: Asia Green Development Bank, Ayeyarwady Bank, Myanmar Economic Bank, and Myanmar Investment and Commercial

Bank. General License No. 19 does not authorize any new investment in or with those four banks,<sup>7</sup> and all property and interest of those four banks in the United States as of the date of the license remain blocked. US financial institutions processing transactions with the four banks are still obligated to conduct enhanced due diligence under section 312 of the USA PATRIOT Act.

Shortly following the issuance of General License No. 19, OFAC published a set of answers to frequently asked questions regarding the Burma sanctions program. This guidance states that US banks are permitted to maintain correspondent banking relationships with both non-blocked banks and the four blocked banks named in General License No. 19. US persons generally remain prohibited from dealing with other blocked banks, including Myanma Foreign Trade Bank, Myawaddy Bank, and Innwa Bank. Further, US persons and financial institutions may not provide financial services related to the provision of security services, directly or indirectly, to the Burmese Ministry of Defense; to any state or non-state armed group; or to any entity in which the foregoing maintain an interest of greater than 50 percent. OFAC's guidance clarifies that the fact that a Burmese governmental minister has been designated by OFAC does not mean the entire government ministry is blocked. The FAQs also state that US persons working on behalf of foreign entities investing in Burma are not subject to the reporting requirements for US persons making new investments in Myanmar.

Except as licensed or otherwise authorized, US persons generally remain prohibited from dealing with blocked persons, which include both persons on the SDN List and any entities 50 percent or more owned by such persons. The prohibitions and restrictions on the importation into the United States of jadeite and rubies, and of articles of jewelry containing them, imposed by the JADE Act amendments to the Burmese Freedom and Democracy Act of 2003 remain in effect.

### New License Reflects Shift in US Policy Towards Syrian Opposition Forces

On March 15, 2013, OFAC issued General License No. 16 authorizing US persons to provide support to the National Coalition of Syrian Revolutionary and Opposition Forces (the "Syrian Opposition Coalition" or "Coalition"), which the US has recognized as the legitimate representative of the Syrian people. This includes the transfer of funds otherwise prohibited under E.O. 13582, "Blocking Property of the Government of Syria and Prohibiting Certain Transactions with Respect to Syria." The license is intended to allow for contributions of funds to aid the Coalition's political organization and reconstruction efforts within Syria. However, any transfer of funds to the Syrian Opposition Coalition must be conducted through the Syrian Opposition Coalition's US offices via a US financial institution that has been specifically licensed to facilitate the transaction. In no case may funds be transmitted to persons who are the targets of US sanctions, including Jabhat al-Nusra, a part of the Syrian rebel coalition that has been listed as a foreign terrorist organization by the US State Department. The license also does not allow for the provision of any services in support of the exportation or re-exportation to Syria of any item listed on the US Munitions List.

<sup>7</sup> "New investment" is defined in 31 CFR 537.311 as including transactions related to (i) the entry into a contract that includes the economic development of resources located in Burma; (ii) the guarantee of such a contract; (iii) the purchase of shares of ownership or an equity interest in the economic development of resources located in Burma; and (iv) the entry into a contract providing for the participation in royalties, earnings, or profits in the economic development of resources located in Burma, without regard to the form of the participation.

## Focus Returns to North Korea as New Sanctions Target the Proliferation of WMDs

Following North Korea's detonation of an underground nuclear device on February 12, 2013, the United Nations Security Council unanimously adopted stringent new sanctions targeting North Korea, which require nations to crack down on North Korean financial transactions and check cargo suspected of containing nuclear and missile-related contraband, actions that before were only voluntary. The export to North Korea of luxury items such as yachts and luxury automobiles is also now banned.

OFAC subsequently designated the Foreign Trade Bank of North Korea (the "FTB"), the country's primary foreign exchange bank, as the target of sanctions pursuant to E.O. 13382, "Blocking Property of Weapons of Mass Destruction Proliferators and Their Supporters." This bars the FTB from doing business with US persons or banks and freezes its assets under US jurisdiction. While North Korean financial institutions have been subjected to US sanctions in the past, those banks, which included Tanchon Commercial Bank and Korea Kwangson Banking, were involved in a much more limited range of activities than the FTB. The Treasury Department has encouraged other nations to follow suit, issuing a March 11 press release urging banks around the world to be wary of the risks of doing business with the FTB.<sup>8</sup> The European Union also expanded its sanctions on North Korea, going beyond those approved by the Security Council by including measures to prevent trading in government bonds, gold, other precious metals, and diamonds. The EU sanctions also bar North Korean banks from opening new branches in the European Union and European banks from opening new branches in North Korea.

In addition to these sanctions specifically targeting North Korea, the US State Department announced on February 11, 2013 the imposition of nonproliferation sanctions on several foreign entities and individuals under multiple US authorities. Pursuant to the Iran, North Korea, and Syria Nonproliferation Act ("INKSNA"), a determination was made to impose sanctions on two Belarusian entities; four Chinese entities and one Chinese individual; two Iranian entities and one Iranian individual; two Sudanese entities; one Syrian entity; and one Venezuelan entity based on information that these persons had transferred to or acquired from Iran, Syria, or North Korea equipment that could materially contribute to those countries' weapons of mass destruction programs. Sanctions were also imposed on a subset of the above-listed persons under the Arms Export Control Act and E.O. 12938. These sanctions bar targeted persons from doing business with or receiving assistance from the US government for a period of two years.

## Treasury and State Department Designations Reflect Terrorism and Human Rights Concerns

Various designations by the Treasury and State Departments throughout the first quarter of 2013 demonstrate that the US remains concerned with the expansion of terrorism in turbulent regions throughout Africa and the Middle East. These designations were made pursuant to E.O. 13224, which targets terrorists and those providing support to terrorists or acts of terrorism and result in an asset freeze and a prohibition on doing business with US persons. Specifically, on January 8, 2013, the State Department designated two Sudanese nationals, Abdelbasit Alhaj Alhassan Haj Hamad and Mohamed Makawi Ibrahim Mohamed, as SDNs under E.O. 13224. Abdelbasit and Makawi were involved in an armed attack in Khartoum, Sudan on January 1, 2008 during which a US diplomat was killed. On February 28, 2013, the State

<sup>8</sup> OFAC also sanctioned Paek Se Bong, chairman of North Korea's Second Economic Committee and a senior member of government. The State Department placed additional sanctions on three individuals linked to North Korea's weapons program: Pak To Chun, the head of the Munitions Industry Department; Chu Kyu Chang, who directs the Munitions Industry Department; and O Kuk Ryul, the vice chairman of the National Defense Commission, which oversees production of ballistic missiles.

Department and OFAC both made designations pursuant to E.O. 13224, including designating Commander Nazir Group, a Pakistani organization believed to train terrorists and to have carried out attacks in Afghanistan; Malang Wazir, the leader of the Commander Nazir Group; and Iyad ag Ghali, the leader of Ansar Dine, a rebel group in Mali. On March 21, 2013, the State Department then designated Ansar Dine as a foreign terrorist organization, citing the group's close cooperation with al-Qaeda in the Islamic Maghreb, al-Qaeda's affiliate in North Africa.

The United States also continues to target human rights violators in Iran, highlighting that the sanctions regime against the Islamic Republic is not solely aimed at preventing the country's development of nuclear weapons. Accordingly, on February 6, 2013, OFAC, in consultation with the State Department, designated the Islamic Republic of Iran Broadcasting and its director, Ezzatollah Zarghami, pursuant to E.O. 13628. E.O. 13628 gives the Treasury Department the authority to designate persons in Iran who restrict or deny the free flow of information to or from the Iranian people. The Iranian Cyber Police, the Communications Regulatory Authority, and Iran Electronics Industries ("IEI") were also designated pursuant to E.O. 13628 for their alleged involvement in censorship within Iran.<sup>9</sup> Thus, any property or interests in property in the United States or in the control of US persons in which the designated persons have an interest are now blocked, and US persons are generally prohibited from engaging in transactions with them.

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As always, we would be happy to discuss with you any questions you may have about compliance with US sanctions programs or trends and patterns in US enforcement.

<sup>9</sup> IEI was designated in September 2008 pursuant to E.O. 13382 for its connections to Iran's development of weapons of mass destruction.