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Sanctions Round-Up: Fourth Quarter 2012

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The final quarter of 2012 was marked by US and EU efforts to prevent Iran from circumventing existing sanctions, an increasingly extraterritorial bent to US sanctions, and record-breaking sanctions-related settlements by foreign financial institutions with US authorities. In the US, the Obama administration worked to implement the numerous provisions of the Iran Threat Reduction and Syria Human Rights Act of 2012 (the "Threat Reduction Act"), signed into law in August of last year, while Congress passed legislation imposing even more expansive sanctions targeting Iran that will go into effect later this year. The US and EU also continued to designate new individuals and entities in Iran and Syria as the targets of sanctions for their involvement in human rights abuses, terrorist activities, and the proliferation of weapons of mass destruction. Finally, while US sanctions targeting Sudan, Cuba, and the old Gaddafi regime in Libya remain in place, the US took action to suspend sanctions targeting Myanmar (Burma) in response to its ongoing efforts at democratic reform, demonstrating that sanctions are not always a one-way ratchet.

Expanded Extraterritorial Reach of Sanctions Targeting Iran

Starting October 9, US companies became liable under the Threat Reduction Act, as implemented by Executive Order ("E.O.") 13628, for sanctionable transactions engaged in with Iran by any non-US entities under their ownership or control. US parent companies will be penalized for such transactions as if they had carried out such transactions themselves, which could include civil fines of up to $250,000 or twice the value of each transaction by their foreign affiliates. However, the Threat Reduction Act has a built-in grace period that allows US companies to escape penalty if they divest or terminate all business by February 6, 2013 with foreign affiliates that continue such sanctioned business after that date.

Revisions to the Iranian Transactions and Sanctions Regulations (the "ITSR") on December 26 implemented this extraterritorial extension of civil penalties. The ITSR are promulgated by the US Treasury Department's Office of Foreign Assets Control ("OFAC") and are intended to consolidate and implement sanctions policies issued by the US government, often clarifying certain sanctions requirements in the process. These December 26 amendments lay out how US companies can avoid penalty through divestment or termination by issuing a new general license that allows for all transactions ordinarily incident and necessary to the winding down of business to be carried out from October 9, 2012 through March 8, 2013 without penalty, so long as those activities do not involve US persons or occur in the United States. The amendments also include another general license that specifies that the foreign affiliates of US companies are authorized to engage in all potentially sanctionable transactions for which the US parent has received specific authorization.

A full description of the applicability of sanctions to non-US persons, including the foreign affiliates of US companies who transact business with Iran, is provided in Shearman & Sterling's client note, "President Obama Issues Executive Order Authorizing Imposition of Sanctions on Non-US Persons who Transact with Iran," dated October 25, 2012.

Guidance for Compliance with New SEC Reporting Requirement

Section 219 of the Threat Reduction Act, codified as section 13(r) of the Securities Exchange Act of 1934, requires disclosure by US issuers of business that it *or any of its affiliates* engage in with Iran or certain Specially Designated Nationals ("SDNs"). This new disclosure requirement generated much chatter and concern following its enactment, due in large part to the lack of specificity regarding the requirement's scope and how it would be enforced. However, on December 4, the Securities and Exchange Commission's ("SEC's") Division of Corporation Finance released its interpretations on the compliance and disclosure issues raised by section 13(r). The SEC staff's interpretations state that for purposes of section 13(r), the term "affiliate" is defined as it is in Exchange Act Rule 12b-2 ("a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, the person specified."). The interpretations also make clear that issuers are required to disclose all activities occurring during the period covered by the report, even if such activities occurred prior to the enactment of the Threat Reduction Act and that issuers may not avoid the required disclosures by filing early, as section 13(r) applies to all reports required to be filed after

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Feb. 6, 2013. A full description of the SEC's interpretations is provided in Shearman & Sterling's client note, "SEC Publishes CD&Is for Iran Sanctions Disclosures Required Under Exchange Act Section 13(r)," dated December 6, 2012.

Further guidance on preparing for this new reporting requirement is detailed in Shearman & Sterling's client publications, "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, 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.

High-Profile US Sanctions Enforcement Actions

In December 2012, US authorities reached a series of record-breaking settlements with global financial institutions related to violations of US sanctions over the past decade. Notably, these settlements included allegations of the use of nontransparent practices, including the stripping of identifying information from SWIFT wire messages to conceal the true nature of the prohibited transactions.

On December 10, Standard Chartered settled for an aggregated $327 million with the Federal Reserve, Department of Justice ("DOJ"), New York District Attorney's Office ("NYDA"), and OFAC after having previously settled with the New York Department of Financial Services ("NYDFS") in August 2012 for $340 million, bringing its total penalties to $667 million. This was immediately followed by the announcement of an HSBC settlement for an aggregated $1.921 billion with the Federal Reserve, DOJ, NYDA, OFAC, and other Treasury Department authorities over allegations of money laundering and violations of multiple sanctions programs, including the movement of hundreds of millions of dollars through the US financial system on behalf of Iranian, Burmese, Sudanese, and Libyan clients. Then, on December 12, Mitsubishi UFJ Financial Group agreed to pay an $8.6 million fine to OFAC for violating US sanctions against transferring funds to accounts held by citizens of Myanmar, Sudan, Iran, and Cuba. In addition to these steep financial penalties, the government imposed a number of ongoing remedial measures on the settling financial institutions, including the expansion of compliance personnel, independent monitoring and reporting to regulatory authorities, and the comprehensive revision of all compliance-related policies and procedures.

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New Sanctions Targeting Iran

The National Defense Authorization Act for FY 2013 ("NDAA 2013"), signed into law on January 2, 2013, bars all transactions with Iran's energy, shipping, and shipbuilding sectors and its ports, designating them as entities of "proliferation concern." Any entity or individual who provides "significant" support for a person designated as part of these sectors or for any Iranian person on the SDN List will likewise be subject to an asset freeze and transaction ban.[1]

The NDAA 2013 also requires the President to impose five or more sanctions under the Iran Sanctions Act ("ISA") on any person[2] and to prohibit correspondent and payable-through accounts by foreign financial institutions for any person determined by the President to have knowingly "conducted or facilitated" a significant transaction for the supply of goods or services used in connection with the energy, shipping, or shipbuilding sectors of Iran, including the National Iranian Oil Company ("NIOC") and the Islamic Republic of Iran Shipping Lines ("IRISL"). The ISA sanctions are explicitly made applicable to underwriters, insurers, and reinsurers, unless such persons can prove they exercised proper due diligence.

The NDAA 2013 includes restrictions on trade in precious metals and materials relevant to Iran's shipbuilding and nuclear programs, including graphite, aluminum, steel, and coal used in those sectors. The President is required to report to Congress whether any material is being used as barter to furnish transactions with Tehran, a provision aimed at preventing Iran's circumvention of sanctions through the barter of oil for precious metals. Finally, the law designates the Islamic Republic of Iran Broadcasting and its president as human rights abusers.

[1] The NDAA 2013 provides an exception for support provided to Iranian financial institutions designated solely with the [IRAN] tag on OFAC's SDN List, which indicates that they are subject to blocking measures in the US. In short, the [IRAN] tag indicates an entity is "blocked" due to the US Government's identification of the entity as the Government of Iran or as an Iranian financial institution. "Designated" persons, in contrast, appear on the SDN List due to their involvement in specific prohibited activities such as the proliferation of weapons of mass destruction or aiding international terrorism. Such entities appear on the SDN List with tags other than [IRAN].

[2] The sanctions available under the ISA include: (1) denial of Export-Import Bank loans, credits, or credit guarantees for US exports to the sanctioned party; (2) denial of licenses for the export of military, dual-use, or nuclear-related goods or technology; (3) denial of US bank loans exceeding $10 million in any 12-month period; (4) prohibition on designation as a primary dealer in US government bonds or on service as a repository for US government funds, if the sanctioned party is a financial institution; (5) prohibition on US government procurement from the sanctioned party; (6) prohibition on foreign exchange transactions subject to US jurisdiction; (7) prohibition on banking transactions subject to US jurisdiction; (8) prohibition on transactions involving any property subject to US jurisdiction in which the sanctioned person has an interest; (9) prohibition on investment in significant amounts of equity or debt instruments of the sanctioned party; (10) denial of visas to corporate officers of companies that violate the ISA; (11) imposition of ISA sanctions on the principal executive officers of companies that violate the ISA; and (12) restrictions on imports from the sanctioned entity.

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Overall, the NDAA 2013 effectively turns entire sectors of the Iranian economy into SDNs, along with any persons providing significant support to those sectors. The NDAA 2013 also appears to lower the bar for the imposition of ISA sanctions, which are currently limited to parties engaged in specific types of transactions that meet certain minimum value thresholds. These new sanctions targeting Iran will go into effect July 1, 2013, although limited 180-day waiver provisions remain available to the President.

Additional Iran-Related Actions

E.O. 13628 of October 9, 2012, noted above, created an overall administrative framework for the new Iranian sanctions signed into law under the Threat Reduction Act by delegating specific powers to the Treasury and State Departments along with other executive agencies to ensure implementation of the Act's numerous statutory provisions. Soon after, on October 22, OFAC issued the ITSR to implement E.O. 13599 of February 5, 2012, entitled "Blocking Property of the Government of Iran and Iranian Financial Institutions," along with the various sanctions provisions contained in the National Defense Authorization Act for FY 2012 ("NDAA 2012"), which was signed into law on December 31, 2011. The newly promulgated ITSR replaced the previously existing Iranian Transactions Regulations in their entirety and contain numerous new prohibitions, definitions, and licensing provisions regarding trade with Iran. Notably, a number of general licenses existing under the Iranian Transactions Regulations have now been removed, and a new prohibition blocks all property of the Government of Iran and any Iranian financial institutions. However, due in part to the expansive scope of this new blocking provision, the ITSR also created general authorizations and specific licenses for certain permitted activities with Iran, including the provision of medicine and medical devices and projects undertaken by nongovernmental organizations.

On November 8, the ITSR were further amended to implement specific sections of the Threat Reduction Act by creating additional categories of activities for which foreign financial institutions may be denied permission to establish correspondent accounts with US financial institutions, including the facilitation of efforts by Iranian financial institutions to support Iran's development of nuclear weapons. As noted above, further amendments to the ITSR on December 26 implemented additional provisions of the Threat Reduction Act and Executive Orders 13522 and 13628, including the expansion of the categories of persons whose US property and interests in property are blocked to include any person determined by the Secretary of the Treasury, in consultation with the Secretary of State, to have materially assisted or provided other support for certain Government of Iran-related entities or certain activities by the Government of Iran.

The US State Department issued guidance on November 13 as to what types of "sensitive technology" US individuals and entities are barred from shipping to Iran and Syria. Under the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 ("CISADA"), US government agencies are barred from entering into or renewing procurement contracts with individuals or entities that export "sensitive technology" to Iran. Additionally, the Threat Reduction Act mandates sanctions on persons determined to have knowingly transferred, or facilitated the transfer of, "sensitive technology" to Iran or Syria. The State Department's guidance acknowledges that while information technology plays a

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role in human rights abuses in Iran and Syria, it also facilitates the flow of information and is used by opposition groups. Thus, the guidance states that the focus will be on technology that could provide "significant surveillance, censorship, or network disruption capabilities to the Iranian or Syrian governments" and will not include basic monitoring capabilities found on smart phones and other common mobile devices. The major factor that the State Department will take into consideration in issuing sanctions is whether a company knew, or should have known, that a particular end-user of its technology was likely to misuse such technology.

A December 10 rule amending the Federal Acquisition Regulations (the "FARs") imposes new restrictions on federal contractors doing business with Iran, as required under the Threat Reduction Act. The FARs are the set of regulations issued by the US federal government to control the process through which the government purchases goods and services. The new rule requires prospective contractors to certify that they, and any persons under their control, do not knowingly engage in significant transactions with Iran's Revolutionary Guard Corps or its agents and affiliates. Contractors making false certifications are subject to a minimum two-year debarment. Due to the existing restrictions on trade with Iran, the rule is expected to have a minimal impact on US entities. However, US companies controlling foreign affiliates trading with Iran could be debarred if those affiliates engage in prohibited transactions.

The US Treasury Department continued to designate individuals and entities to its SDN List throughout the fourth quarter of 2012, targeting those persons involved not only in Iran's attempts to develop weapons of mass destruction but also those complicit in human rights abuses and terrorism. For example, on October 18, the Treasury Department designated Adel Radi Sagr al-Wahabi al-Harbi as an SDN pursuant to E.O. 13224, which targets terrorists and terrorist organizations, due to his involvement in al Qaeda's network in Iran. On November 8, another four individuals were designated under E.O. 13224 for their ties to Kata'ib Hizballah, a foreign terrorist organization operating out of Iran and Iraq that is alleged to engage in acts of violence threatening the stability of Iraq. An additional four Iranian officials and five organizations were designated under E.O. 13628 for their involvement with jamming satellite broadcasts and blocking Internet access for Iranian citizens, while four entities were designated under E.O. 13382 for supporting Iran's Revolutionary Guard Corps ("IRGC") and its proliferation-related activities. On December 13, the Treasury Department further targeted Iran's uranium enrichment program by imposing sanctions on seven companies and five individuals, including Iran's atomic energy chief, pursuant to E.O. 13382; another four companies and one person were designated pursuant to the same Executive Order on December 21. Persons designated to the SDN List have their US assets frozen and are banned from doing business in the US or with US persons. Additionally, under CISADA, foreign banks that handle transactions for those companies and individuals designated for their involvement in specific activities, including terrorism or the proliferation of weapons of mass destruction, could also lose their access to the US banking system.

The United States requires the countries that are major buyers of Iranian crude oil to progressively cut their imports to secure exceptions to sanctions, which are subject to review every 180 days. On December 7, the US granted 180-day renewals of waivers from sanctions targeting Iran oil transactions to China, India, South Korea, South Africa, Turkey, Sri Lanka, Malaysia, Singapore, and Taiwan in exchange for their cutting purchases of oil from Iran. Waivers for all twenty

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of Iran's major oil buyers have now been renewed for a second time. Notably, countries that have received such waivers will, as of February 6, 2013, only be permitted to pay for crude oil from Iran using a bank within their own country, and only if the money is used to facilitate permitted trade between that country and Iran. The money may not be transferred to third countries, repatriated to Iran, or used to facilitate trade with third countries.

On December 28, President Obama signed into law the "Countering Iran in the Western Hemisphere Act of 2012," which requires the US State Department to develop a strategy within 180 days to address Iran's increasing presence and "hostile" activity in Latin America. This strategy must include an analysis of Iran's relationships with governments and other actors in the region and proposals on how US resources could be utilized to address attempts to aid Iran in illicit activities in the region, including the evasion of economic sanctions.

The US has set a March 2013 deadline for Iran to begin cooperating in substance with the International Atomic Energy Agency's ("IAEA's") investigation into its uranium enrichment activities, warning that it will refer the issue to the UN Security Council. The IAEA is scheduled to meet with Iranian officials again in January despite an apparent lack of progress. Although both Iran and the negotiating bloc of China, France, Germany, Russia, the United Kingdom, and the United States (known as the "P5+1") have stated their desire to re-engage in nuclear-focused talks, such talks have been stalled for months, and no new date or location for negotiations has yet been announced.

In the European Union, expanded sanctions targeting Iran were agreed to on October 15, including the imposition of a blanket ban on financial transactions between European and Iranian banks absent explicit advance approval by national authorities; such approval will be strictly limited to cases of humanitarian need or certain cases of legitimate trade. The EU previously had broadly allowed such transactions unless specifically banned. The new measures also broaden the EU energy embargo that came into effect in July 2012 through a ban on the importation, purchase, or transport of natural gas from Iran. Exports of a range of goods used to support Iran's nuclear program, including graphite, raw metals, naval and shipbuilding equipment, software, and key equipment for the oil, gas, and petrochemical industries are also now prohibited, along with the provision of related technical or financial assistance. Trade with Iran is further limited by a ban prohibiting European governments from extending short-term trade guarantees, credits, or insurances. Finally, the flagging or classification of Iranian tankers and cargo is now banned, along with the provision of storage or transport vessels for Iranian crude oil or petrochemical products. International shipping databases show that the state-controlled Islamic Republic of Iran Shipping Lines has repeatedly shifted the flag registration of a number of its vessels in recent months to disguise their identities as entities subject to EU and US sanctions. The implementing legislation for these new EU sanctions was approved on December 21.

Further, the EU named thirty-four Iranian entities and one individual as additional targets for asset freezes on October 15, including the National Iranian Oil Company ("NIOC"), the National Iranian Tanker Company ("NITC"), and NIOC subsidiaries such as Naftiran Intertrade Company and the National Iranian Gas Company. Several Iranian banks were also added to the blacklist, along with Iran's energy minister. In coordinated action with the US, the EU also increased the

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number of blacklisted companies and individuals linked to the Iranian nuclear program on December 21, targeting eighteen companies and one individual with an asset freeze and travel ban. This brings the total number of entities subject to EU sanctions to 490 and the total number of people to 105. However, on December 11, the European Court of Justice ordered the EU to lift sanctions against Iranian private bank Sina following legal action by the bank, finding that the documents and evidence allegedly proving the bank's involvement in activities related to Iran's nuclear program were groundless.

Syria-Related Updates

As noted above, the US State Department issued guidance on November 13 as to what types of "sensitive technology" US individuals and entities are barred from shipping to Iran and Syria. Additionally, the US Treasury Department continued to designate individuals to the SDN List for their involvement in human rights abuses and terrorist activities in Syria. On December 11, the Treasury Department designated Jabhat al-Nusra, a Syrian opposition militia that includes hundreds of foreign fighters, and imposed sanctions on its leaders for their alleged ties to al Qaeda in Iraq. The State Department simultaneously designated al-Nusra as a terror group. The Treasury Department also blacklisted two pro-Assad militias and their commanders, including a militia jointly developed by the Syrian government and Iran's Islamic Revolutionary Guard Corps. On December 17, the Treasury Department sanctioned former Lebanese Minister of Information and Tourism Michel Samaha under E.O. 13441, which targets people undermining Lebanese sovereignty, for providing support to Assad's efforts to de-stabilize Lebanon; the State Department simultaneously named Samaha as a global terrorist under E.O. 13224.

In the European Union, travel bans and assets freezes were imposed against an additional twenty-eight Syrian officials, along with two Syrian entities, bringing the total number of blacklisted companies and individuals to 235. The EU also prohibited the import into the EU of arms from Syria or any other EU involvement in the transport of Syrian arms, including the provision of financial services, insurance, or re-insurance for Syrian arms exports. The EU also denied access to all flights operated by Syrian Arab Airlines, extending what previously had been a ban on Syrian cargo flights. On November 28, the EU extended sanctions against the Syrian regime for another three months. This three-month renewal was a reduction from the expected year-long renewal, a change that will allow the EU to more frequently review the sanctions and make amendments, including those that would potentially allow the supply of training and equipment to the Syrian rebels.

Libya-Related Updates

On October 18, the US Treasury Department imposed a travel ban and assets freeze pursuant to E.O. 13566 against a South African woman for allegedly moving money to aid Saadi Gaddafi, the son of former Libyan leader Muammar Gaddafi. While the majority of sanctions targeting Libya were lifted in December 2011 following the regime's downfall,

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sanctions on Gaddafi's regime and its associates under E.O. 13566 of March 1, 2011 remain in place, aimed at preventing Libyan state assets from being misappropriated.

On October 14, Libya's national congress elected a new prime minister, Ali Zidan; the previous prime minister was dismissed in early October after failing to form a government. Zidan then gained the support of the National Congress for his choice of ministers, including a coalition of liberal figures and Islamists, on October 31. Libya's parliament has ordered the temporary closure of southern borders and declared seven southern regions restricted military areas in a move aimed at preventing the flow of illegal immigrants and goods into the country. The parliament gave no indication of how long borders with Chad, Niger, Sudan, and Algeria would remain shut. Libya's southern regions have struggled with lawlessness since the overthrow of Colonel Gaddafi's regime in 2011. Libya also began the trial of former Prime Minister al-Baghdadi al-Mahmoudi, who is charged with acts contributing to the unjust killings of Libyan citizens. Mahmoudi and two others are also accused of channeling millions in public funds through Tunisia to help forces supporting Gaddafi. Mahmoudi is one of four senior officials from the former government being prosecuted in Libya. The one-year anniversary of Gaddafi's capture was marked on October 20, 2012.

Myanmar (Burma)-Related Updates

On October 5, President Obama signed H.R. 6431, a bill intended to provide the US administration with the flexibility to determine, in the national interest, whether to support the provision of assistance by international financial institutions to Myanmar. The new legislation will make it easier for the United States to back international financial institutions by empowering US authorities to vote in favor of financial assistance to Myanmar upon the direction of the president.

In a joint action by the US State and Treasury Departments on November 16, the Obama administration authorized the importation of Myanmar-origin goods into the United States for the first time in almost a decade. The State Department's waiver of the import ban required under the Burmese Freedom and Democracy Act of 2003 and E.O. 13310 was followed by the Treasury Department's issuance of General License 18, which broadly authorizes imports to the US from Myanmar. Neither the waiver nor the license affect standing prohibitions and restrictions on the importation of jadeite and rubies mined or extracted from Myanmar and on articles of jewelry containing them, imposed under the Tom Lantos Block Burmese JADE Act of 2008. US individuals and entities are also still prohibited from engaging in transactions with persons on the SDN List, along with any entity in which an SDN owns, directly or indirectly, a 50 percent or greater interest. Despite this easing of the import ban, the underlying legal regime for sanctions against Myanmar remains in place, and the Obama administration has stated its intention to continue to monitor the country's progress on implementing reforms. Additionally, the Treasury Department simultaneously announced the designation of seven entities alleged to be front companies for members of the previous Myanmar regime. The Obama administration and human rights groups continue to raise concerns about ongoing violence between the Muslim Rohingya minority and Buddhists in the western region of the country.

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In November, the Myanmar government signed into law a long-anticipated foreign investment bill. While details of the law have not yet been published, the law purportedly removes a 50 percent cap on foreign holdings, allowing the exact investment ratio to be decided by foreign and local partners. The law also offers tax breaks and allows for lengthy land leases to overseas companies. Full rules and regulations to implement the bill are to be issued within the next few months. Further, the World Bank announced its approval of an $80 million grant to Myanmar and pledged lending to the country for the first time in twenty-five years. The money is to be spent on building roads, bridges, schools, and health clinics in rural communities. An additional $165 million will be made available once the country clears its overdue debt to the Bank.

Sudan-Related Updates

In mid-October, the Sudanese parliament ratified a deal with South Sudan settling numerous disputes arising from South Sudan's recent secession, a move that led South Sudan to order its oil companies to restart production after a months-long hiatus. However, on November 2, President Obama renewed US sanctions targeting Sudan, keeping in place restrictions on trade and investment in Sudan, along with the current freeze on the assets of certain Sudanese officials, that have been imposed under E.O. 13067 since 1997. President Obama acknowledged Sudan's recent resolution of disputes with South Sudan but pointed to ongoing violence in Darfur and Sudan's southern border regions as part of the actions and policies of Sudan that continue to pose a threat to the national security and foreign policy of the United States.

Cuba-Related Updates

In mid-October, Cuba announced that, starting in January 2013, it will allow residents to leave the country without first obtaining official exit permits, a process that has proved to be both lengthy and expensive. Cuban citizens will also be allowed to stay abroad for up to twenty-four months, instead of the current eleven. However, highly qualified professionals such as doctors will continue to face travel controls, and required passport updates may be denied for "reasons of public interest defined by the authorities."

While the re-election of President Obama has sparked speculation over how US policy toward Cuba may change during his second term, Cuba's continued detention of US citizen Alan Gross, jailed in 2011 for charges arising from bringing internet equipment to the island, is seen as a major obstacle to any attempts to improve US-Cuban relations.

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