

KIRKLAND ALERT

May 2012

United States Implements Multi-Pronged Expansion of Iran and Syria Sanctions

In recent months, the United States has announced multiple measures that expand once again U.S. sanctions targeting the governments of Iran and Syria. On May 1, 2012, President Obama issued an Executive Order that punishes foreign parties seeking to evade Iran and Syria sanctions by barring such “sanctions evaders” from engaging in any commercial interactions with U.S. parties and from entering into the United States or its territories. Financial sanctions imposed a few months earlier have begun to impact foreign markets, causing other governments to express concern that these rules could exclude foreign financial institutions from the U.S. financial system and overly restrict access to Iran’s oil market. Additional measures sanction the provision of technology that could assist the governments of Iran or Syria in engaging in surveillance and related human rights abuses of their citizens. At the same time, protections intended to benefit ordinary Iranian citizens — authorization of certain no-fee Internet and media communications services and related software — have been clarified.

I. Executive Order Paves Way for Designation of “Evaders” of Iranian and Syrian Sanctions

On May 1, 2012, President Obama issued **Executive Order 13608**, “Prohibiting certain transactions with and suspending entry into the United States of foreign sanctions evaders with respect to Iran and Syria,” which establishes a separate designation category for non-U.S. parties that violate or purposefully evade Iran and Syria sanctions. Designated “sanctions evaders” may be effectively cut off from the U.S. market.¹ This authority provides a more expedient and direct method of penalizing non-U.S. parties that violate U.S. sanctions and may otherwise be difficult to bring within the jurisdictional reach of existing U.S. civil and criminal processes.

The Order calls upon the Secretary of the Treasury, in consultation with the Secretary of State, to designate any foreign person who:

- i. has “violated, attempted to violate, conspired to violate, or caused a violation” of myriad sanctions related to Executive Orders targeting Iran or Syria;
- ii. has “facilitated deceptive transactions” for or on behalf of any person subject to U.S. sanctions targeting Iran or Syria; or
- iii. is “owned or controlled by, or is acting or purporting to act for or on behalf of,” directly or indirectly, any person determined to meet the above criteria.²

Generally, Executive Order 13608 relates to sanctions regulations targeting Iran and Syria administered by the U.S. Department of the Treasury, Office of Foreign Assets Control (“OFAC”), including anti-terrorism and weapons of mass destruction (WMD) proliferation sanctions as they relate to Iranian- or Syrian-sanctioned entities.³ A “deceptive transfer” is defined to include “any transaction where the identity of any person subject to United States sanctions concerning Iran or Syria is withheld or obscured from other participants in the transaction or any relevant regulatory authorities.” Had such designation authority existed previously, major non-U.S. financial institutions that paid large fines in recent years for stripping the identity of OFAC-sanctioned parties or countries from transactions routed through U.S. financial institutions may have been designated as “sanctions evaders.”

The Secretary of the Treasury is authorized to prohibit U.S. persons from “all transactions or dealings, whether direct or indirect, involving” any party designated under Executive Order 13608, including any “exporting, reexporting, importing, selling, purchasing, transporting, swapping, brokering, approving, financing, facilitating, or guaranteeing” of any goods, services, or technology.⁴ In addition, designated “sanctions evaders” are prohibited from entering the United States.⁵

The Order significantly increases the breadth and potential impact of U.S. sanctions against non-U.S. entities that are doing business with Iran and Syria by threatening isolation from U.S. markets. This expansion of U.S. sanctions targeting Iran and Syria follows several other recent announcements also expanding these sanctions regimes as detailed below.

II. U.S. Law Targets Activities of Non-U.S. Sovereign and Commercial Financial Institutions to Increase Pressure on Iranian Regime

On December 31, 2011, U.S. sanctions against Iran were signed into law as part of the **National Defense Authorization Act for 2012 (HR 1450)** (“NDAA”). These sanctions generally: (i) expand the reach of U.S. sanctions and curtail or deny non-U.S. financial institutions access to the U.S. financial system for engaging in certain “significant transactions” with Iranian financial institutions, with certain exceptions applying to transactions involving Iranian oil or other petroleum products; (ii) block any property or interest in property of Iran’s entire financial sector, including the Central Bank of Iran (“CBI”); and (iii) declare the entire Iranian financial sector, including CBI, to be a “jurisdiction of primary money laundering concern.”

A. Non-U.S. Financial Institutions With Iranian Ties May Risk Exclusion from the U.S. Market

In an expansion of existing Iranian sanctions, the NDAA prohibits or limits U.S. financial institutions’ ability to maintain any correspondent account or payable-through account by a non-U.S., or “foreign,” financial institution that “has knowingly conducted or *facilitated any significant* financial transaction” (emphasis added) with banned parties (including CBI) as well as other designated Iranian financial in-

stitutions on the Specially Designated Nationals (“SDN”) and Blocked Persons List administered by OFAC. This determination process authorizes the president to cut off private-sector foreign financial institutions from a significant portion of the U.S. financial system by listing the foreign institutions on a separate list of aiders and abettors of Iranian Interests (*see* section II.C. below).⁶

In making this determination, the definitions of “facilitation” and “significant” financial transactions are key. OFAC has in the past interpreted the concept of “facilitation” very broadly in the context of many of its other sanctions regulations to indicate activity, other than clerical, in furtherance of a sanctioned act.⁷ A February 14, 2012, OFAC guidance noted that the question of “facilitation” would be a case-by-case determination, but financial institutions will want to scrutinize carefully any dealings that could be construed as “facilitating” the business of Iranian clients targeted by these measures. The same guidance notes that OFAC will not sanction foreign banks for holding Iranian assets in accounts opened in 2011 or earlier that are currently frozen, with “ordinary commercial interest payments and routine roll-overs of time deposits under pre-existing instructions being the only new transactions.”⁸

OFAC has provided additional guidelines regarding what transactions may be viewed as “significant.” According to its regulations, factors used to determine whether such transactions are “significant” include the size, number, frequency, and nature of the transactions, the involvement by management, whether the transactions were entered into as part of a pattern of conduct (as opposed to being an active business decision), the proximity or relationship between the foreign financial institution and the sanctioned party, whether deceptive practices were employed to disguise the transaction, and the impact of the transaction on U.S. national interests.⁹ These factors leave considerable room for OFAC to exercise discretion.

The NDAA authorizes the imposition of penalties for violation of these provisions, leaving to the president’s discretion pursuant to the broad authorities of the **International Emergency Economic Powers Act (“IEEPA”)**¹⁰ the form that those sanctions may take. IEEPA current penalties provide for:

- Civil penalty fines of up to \$250,000 or twice the value of the transaction for each violation; and
- Criminal penalty fines of up to \$1 million and up to 20 years imprisonment for individuals.

A single transaction may involve multiple violations. Conspiring to violate and causing a violation also constitute violations.¹¹ President Obama recently imposed sanctions under this authority (*see* section D below).

B. Financial Institutions, Including Government-Owned Institutions, Risk Similar Exclusion from U.S. Markets for Petroleum-Related Transactions in Most (but Not All) Foreign Countries

The NDAA sanctions on foreign financial institution transactions will only apply to government-controlled entities, including central banks, engaging Iran in the purchase or sale of petroleum or petroleum-based products.¹² But before authorizing any oil-related sanctions, including against private financial institutions, the president must determine that there are sufficient alternative sources of oil to avoid unduly burdening other countries' oil supplies.¹³ This requirement was satisfied on March 30, 2012, when President Obama made this determination, finding among other things that:

[G]iven current global economic conditions, increased production by certain countries, the level of spare capacity, and the existence of strategic reserves, among other factors, I determine, pursuant to section 1245(d)(4)(B) and (C) of the [NDAA], that there is a sufficient supply of petroleum and petroleum products from countries other than Iran to permit a significant reduction in the volume of petroleum and petroleum products purchased from Iran by or through foreign financial institutions.¹⁴

The NDAA also authorizes a waiver of these sanctions for countries that have significantly reduced their oil purchases from Iran.¹⁵ In the exercise of this discretion, on March 18, 2012, Secretary of State Hillary Clinton announced that the administration would **waive imposition of these sanctions against Bel-**

gium, the Czech Republic, France, Germany, Greece, Italy, Japan, the Netherlands, Poland, Spain, and the United Kingdom, through September 16, 2012 (with a possibility of renewal).¹⁶ All other countries' government-owned institutions, notably including those in China, India, and Russia, are subject to potential sanctions as described in the prior section.

C. Revised Regulations Reflect Violators of NDAA Financial Sector Sanctions

On March 27, 2012, OFAC amended the **Iranian Financial Sanctions Regulations ("IFSR")** to reflect new NDAA rules. The IFSR were first passed to implement Section 104(c) of the **Comprehensive Iran Sanctions And Divestment Act ("CISADA")** and prohibit U.S. financial institutions from opening certain accounts for any foreign financial institution that assists the CBI (or any other Iranian financial institution) in efforts to acquire weapons of mass destruction or support international terrorism.

The changes to the IFSR pursuant to the NDAA include updated reporting requirements and a new list of non-Iranian foreign entities that are found to have dealt with Iranian entities.¹⁷ The list will be added to the existing IFSR Annex list established pursuant to CISADA. Violations of these prohibitions are subject to IEEPA penalties (*see* above).

D. Foreign Party Accounts at U.S. Financial Institutions Face Increased Scrutiny Under the USA Patriot Act Section 311

With the passage of the NDAA, enhanced diligence requirements imposed by Section 311 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism ("USA PATRIOT") Act of 2001 will apply to U.S. financial institutions to prevent dealings with any part of the Iranian financial sector, including CBI. The NDAA¹⁸ declared the entire Iranian financial system, to include CBI, as a "jurisdiction of primary money laundering concern" pursuant to section 311.¹⁹ This declaration follows and supersedes the U.S. Treasury Department, Financial Crimes Enforcement Network (FinCEN) proposed regulations of November 21, 2011, (*please see [Kirkland Client Alert of December 2011](#)*) to make the Iranian financial system a "jurisdiction of primary money laundering concern."²⁰

Section 311 generally authorizes the secretary of the treasury to require U.S. financial institutions to take special steps to ensure that they do not deal with funds related to any parties designated under Section 311 as “of primary money laundering concern.” These steps include enhanced reporting, information retention, and customer identification and restrictions.

E. Blocking of Property and Interest in Property of CBI and All Other Iranian Financial Institutions

In addition to potential sanctions on non-U.S. persons for “significant” transactions with the Iranian financial sector, the NDAA also authorizes the freezing of all property and interests in property of all Iranian financial institutions that come into U.S. possession or control.²¹ Previously, only certain institutions designated on OFAC’s SDN List were subject to such blocking.

President Obama implemented this particular provision on February 5, 2012, by issuing **Executive Order 13599**, “Blocking the Property of the Government of Iran and Iranian Financial Institutions.”²² This Order is effective as of February 6, 2012, and provides that all property and interests in property of the government of Iran and any Iranian financial institution, “including the Central Bank of Iran,” that are in the United States or come within the possession or control of any U.S. Person, are blocked and “may not be transferred, paid, exported, withdrawn, or otherwise dealt in.” Additionally, all property and interests in property of any person “determined by the secretary of the treasury, in consultation with the secretary of state, to be owned or controlled by, or to have acted or purported to act for or on behalf of, directly or indirectly, any person whose property and interests in property are blocked” pursuant to the Order also will be blocked. Potential penalties are pursuant to IEEPA (*see above*).

III. Promoting Public Use of Software, Internet and Communications Technologies in Iran and Syria

Separately from the NDAA, the United States has taken actions in the last several weeks that target the use of technology related to Iran and Syria. One measure’s stated aim is to ensure that U.S. technology companies are not discouraged from providing technology tools for the widespread use of networking and communication software by ordinary citizens of Iran.

On the other side, parties that assist Iranian or Syrian governmental authorities in their use of technology to control their citizens are subject to potential designation on OFAC’s SDN List.

A. OFAC Clarifications Seek to Maintain Active Flow of Communications Software from U.S. Companies to Iranian Citizenry

After many companies stopped all software exports to Iran in the wake of new OFAC regulations restricting transactions with Iran, **OFAC on March 29, 2012, issued an interpretive guidance and new licensing policy** clarifying its position on certain communications technology and related software exports to Iran.²³ The guidance specifically notes certain technologies whose export is not covered by Iranian sanctions.

In a March 2010 rule, OFAC already explicitly allowed for the export to Iran of all goods “incident to the exchange of personal communications over the Internet, such as instant messaging, chat and email, social networking, sharing of photos and movies, web browsing, and blogging,” as well as enabling software thereof,²⁴ so long as such software was made available free to all users, and was classified as “EAR99” or “5D992” under the Export Administration Regulations (EAR).²⁵ However, OFAC issued the 2012 guidance in response to apparent confusion over the technologies that were covered by this rule.

As the new OFAC guidance explains, to ensure further that Iran sanctions do not prevent the availability of personal communications software in Iran to the general populace, OFAC officially set out a list of “compliant” software that can be exported freely to Iran. This list includes:

- Personal Communications (e.g., Yahoo Messenger, Google Talk, Microsoft Live, Skype (non-fee based));
- Updates to Personal Communications Software;
- Personal Data Storage (e.g., Dropbox);
- Browsers/Updates (e.g., Google Chrome, Firefox, Internet Explorer);
- Plug-ins (e.g., Flashplayer, Shockwave, Java);

- Document Readers (e.g., Acrobat Reader);
- Free Mobile Apps Related to Personal Communications; and
- RSS Feed Readers and Aggregators (e.g., Google Feed Burner).²⁶

The guidance also specifies that services such as web hosting, online advertising, fee-based mobile apps, and fee-based Internet communications, are also acceptable; and it defines all of these terms for further clarity.²⁷

B. New Executive Order Targets Parties Assisting in Internet- or Communications-Based Activities by Iranian and Syrian Governments That Could Contribute To Human Rights Abuses

To combat Iranian authorities' use of technology to

oppress its citizenry, President Obama on April 22, 2012, issued **Executive Order 13606**, blocking all assets of, as well as entry into the United States by, parties conducting or assisting in information technology-based human rights abuses by Iran.²⁸ The Order is most concerned with the use of "information and communications technology that facilitates computer or network disruption, monitoring, or tracking that could assist in or enable serious human rights abuses by or on behalf of the Government of Iran," and targets all parties who have directed, sold goods likely to be used to perpetrate, or "materially assisted" with such activities.²⁹ The president designated certain parties under the Order. That list currently includes the following Iranian entities: Ministry of Intelligence and Security (MOIS), Islamic Revolutionary Guard Corps (IRGC), Law Enforcement Forces (LEF), and Datak Telecom. It also includes the following Syrian entities: Ali Mamluk, director of the Syrian General Intelligence Directorate, Syrian General Intelligence Directorate, and Syriatel.³⁰

¹ Executive Order Prohibiting Certain Transactions With and Suspending Entry Into the United States of Foreign Sanctions Evaders With Respect to Iran and Syria, May 1, 2012.

² *Id.* § 1(a).

³ The Order covers all executive sanctions based on previous declarations of national emergencies in Iran (Executive Order 12957, March 15, 1995) and Syria (Executive Order 13338, May 11, 2004). It also covers violations of broader executive orders designed to prevent WMD proliferation activities and the promotion of terrorism, although only as such violations "relate[] to property and interests in property of" persons targeted by Iran- or Syria-specific sanctions. *Id.*

⁴ *Id.* § 1(b).

⁵ *Id.* §§ 3, 4.

⁶ Section 1245(h) provides that "foreign financial institution" is to be interpreted by the U.S. Secretary of the Treasury (pursuant to the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (22 U.S.C. 8513(i)), which in other recent Iranian sanctions regulations (31 C.F.R. 561.308) has defined the term to mean:

any foreign entity that is engaged in the business of accepting deposits, making, granting, transferring, holding, or brokering loans or credits, or purchasing or selling foreign exchange, securities, commodity futures or options, or procuring purchasers and sellers thereof, as principal or agent. It includes but is not limited to depository institutions, banks, savings banks, money service businesses, trust companies, securities brokers and dealers, commodity futures and options brokers and dealers, forward contract and foreign exchange merchants, securities and commodities exchanges, clearing corporations, investment companies, employee benefit plans, and holding companies, affiliates, or subsidiaries of any of the foregoing. The term does not include the international financial institutions identified in 22 U.S.C. 262r(c)(2), the International Fund for Agricultural Development, or the North American Development Bank.

⁷ See e.g., 31 C.F.R. Parts 537, 538 and 560.

⁸ OFAC Guidance, Feb. 14, 2012.

⁹ 31 C.F.R. § 561.404, as updated by *Iranian Financial Sanctions Regulations*, 77 Fed. Reg. 11724 (Feb. 27, 2012).

¹⁰ 50 U.S.C. § 1701 et seq.

¹¹ Section 1245(g) of NDAA.

¹² Section 1245(d)(3) of NDAA.

- ¹³ Section 1245(d)(4) of NDAA.
- ¹⁴ Presidential Determination Pursuant to Section 1245(d)(4)(B) and (C) of the National Defense Authorization Act for Fiscal Year 2012, Presidential Determination No. 2012-05 (Mar. 30, 2012), *available at* <http://www.gpo.gov/fdsys/pkg/DCPD-201200229/pdf/DCPD-201200229.pdf>.
- ¹⁵ Section 1245(d)(4)(C) of NDAA.
- ¹⁶ Department of State Statement, Mar. 20, 2012.
- ¹⁷ 31 C.F.R. §§ 561.201(a), (b); 75 Fed Reg. 49836, 49839 (Aug. 16, 2010).
- ¹⁸ Section 1245(b) of NDAA.
- ¹⁹ 31 U.S.C.. § 5318(A).
- ²⁰ *Financial Crimes Enforcement Network, Finding That the Islamic Republic of Iran Is a Jurisdiction of Primary Money Laundering Concern*, 76 Fed. Reg. 72756 (Nov. 25, 2011); *Financial Crimes Enforcement Network, Amendment to the Bank Secrecy Act Regulations-Imposition of Special Measure Against the Islamic Republic of Iran as a Jurisdiction of Primary Money Laundering Concern*, 76 Fed. Red. 72878 (Nov. 28, 2011).
- ²¹ Section 1245(c) of NDAA.
- ²² The EO is available at <http://www.whitehouse.gov/the-press-office/2012/02/06/executive-order-blocking-property-government-iran-and-iranian-financial-> (last visited Feb. 13, 2012).
- ²³ U.S. Dept. of the Treasury, Office of Foreign Assets Control, Iranian Transactions Regulations Interpretive Guidance and Statement of Licensing Policy on Internet Freedom in Iran, *available at* http://www.treasury.gov/resource-center/sanctions/Programs/Documents/internet_freedom.pdf [hereinafter OFAC Interpretive Guidance on Internet Freedom].
- ²⁴ 31 C.F.R. part 560.540; see also 75 Fed. Reg. 10997, March 10, 2010).
- ²⁵ 31 C.F.R. part 560.540(a).
- ²⁶ OFAC Interpretive Guidance on Internet Freedom, *supra* note 18.
- ²⁷ *Id.*
- ²⁸ Executive Order Blocking the Property and Suspending Entry into the United States of Certain Persons with Respect To Grave Human Rights Abuses by the Governments of Iran and Syria via Information Technology, Apr. 23, 2012
- ²⁹ *Id.* §1(a)(ii).
- ³⁰ *Id.* § 1(a)(i), Appendix.

If you have any questions about the matters addressed in this *Kirkland Alert*, please contact the following Kirkland authors or your regular Kirkland contact.

Laura L. Fraedrich
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/lfraedrich
+1 (202) 879-5990

Joanna M. Ritcey-Donohue
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/jritcey-donohue
+1 (202) 879-5980

Gregory E. Wannier
Kirkland & Ellis LLP
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/gwannier
+1 (202) 879-5909

This communication is distributed with the understanding that the author, publisher and distributor of this communication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use. Pursuant to applicable rules of professional conduct, this communication may constitute Attorney Advertising.

© 2012 KIRKLAND & ELLIS LLP. All rights reserved.

www.kirkland.com