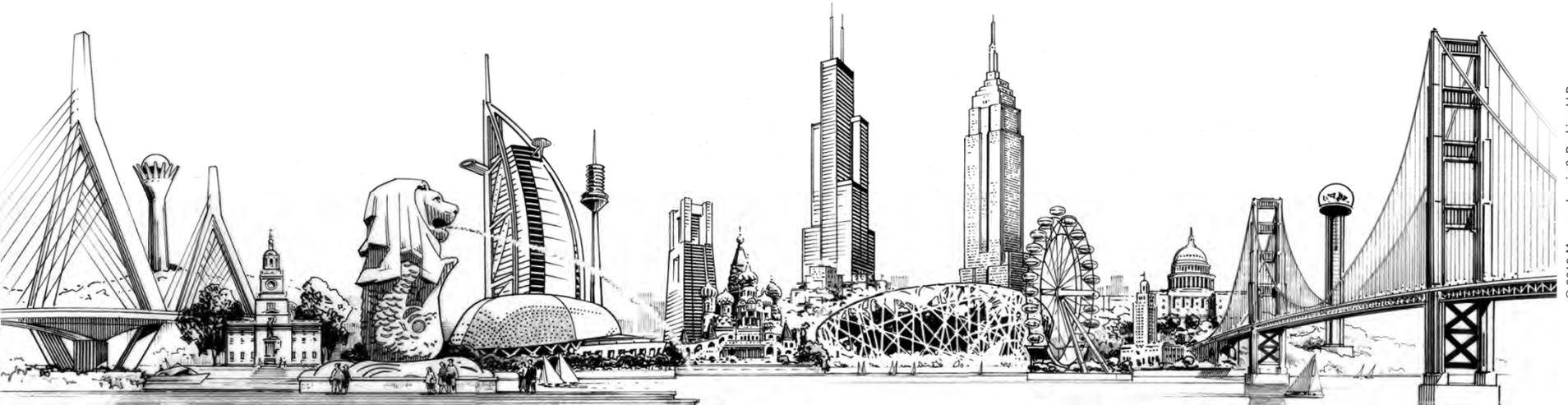


Morgan Lewis

NAVIGATING BETWEEN U.S. IRAN SANCTIONS AND THE E.U. BLOCKING STATUTE

Stefan Reisinger and Nicola Kelly
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INTRODUCTION

United States:

"Anyone doing business with Iran will NOT be doing business with the United States"

- President Donald J. Trump, August 7, 2018

European Union:

"If EU companies abide by U.S. secondary sanctions, they will, in turn, be sanctioned by the EU."

- Spokeswoman for E.U. Foreign Policy Chief Federica Moherini, August 7, 2018

AGENDA

- I. Brief Overview of U.S. Iran Sanctions
- II. Withdrawal from the JCPOA
- III. Executive Order 13846
- IV. European Blocking Statute (“Blocking Statute”)
- V. Practical Considerations

OVERVIEW OF US IRAN SANCTIONS

- The United States has maintained sanctions on Iran since the Islamic revolution in 1979.
- Consist of **primary sanctions** that apply to U.S. persons and foreign entities owned or controlled by U.S. persons as well as **secondary sanctions** that apply to activities by foreign companies regardless of a U.S. nexus.
- Implemented by multiple statutes and executive orders. For example, secondary sanctions legislation includes:
 - Countering America’s Adversaries Through Sanctions Act (CAATSA)
 - **Iran Sanctions Act of 1996 (“ISA”)**
 - Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (“CISADA”)
 - **National Defense Authorization Act for FY 2012 (“NDAA”)**
 - **Iran Threat Reduction and Syria Human Rights Act of 2012 (“ITRA”)**
 - **Iran Freedom and Counter Proliferation Act (“IFCPA”)**
 - **Iranian Transactions and Sanctions Regulations (“ITSR”)**
 - Various Executive Orders

** Items in bold are covered by the Blocking Statute*
- Centered on Iran’s human rights abuses, nuclear development ambitions, support of terrorist organizations, and ballistic missile programs.
- Overseen by the U.S. Department of Treasury, Office of Foreign Assets Control (OFAC).
- OFAC has also designated hundreds of individuals and entities in Iran to its Specially Designated and Blocked Persons List (“SDN List”).
 - U.S. persons must block the assets of SDNs and are generally prohibited from engaging in any transactions in which they are directly or indirectly involved.

NUCLEAR AGREEMENT WITH IRAN – THE JCPOA

- In July, 2015 the P5+1 (China, France, Germany, Russia, the United Kingdom, and the United States) entered into a joint comprehensive plan of action (“JCPOA”) with Iran whereby Iran agreed to temporarily suspend its nuclear program in exchange for limited relief from sanctions.
 - Extended multiple times.
 - Had no impact on U.S. primary sanctions on Iran other than pursuant to General License H.
- Provided for the suspension or reduction of U.S. **nuclear related** secondary sanctions but left in place secondary sanctions related to Iran’s development of ballistic missile and other weapons programs, human rights abuses, and support for terrorism.
- In particular, the JCPOA relaxed sanctions on transactions involving Iran’s:
 - Energy, petrochemical, shipping, shipbuilding, and automotive Sectors
 - Purchase and sale of gold and other precious metals
 - Civil aviation industry
 - Humanitarian related transactions
 - Related insurance and financial transactions
- Also suspended the designation of numerous individuals and entities on OFAC’s SDN List.
- Did not remove the core U.S. sanctions on foreign entities that engage in transactions with Iran related to petroleum (crude) or petroleum products.
 - During the JCPOA Period, however, the U.S. agreed to “pause” efforts to further reduce Iran’s crude oil sales by enabling China, India, Japan, South Korea, Taiwan and Turkey to keep purchasing their then current average amounts of crude oil from Iran without being subjected to sanctions.

NUCLEAR AGREEMENT WITH IRAN, CONT'D

- **General License H** (issued on January 16, 2016): authorized US-owned or controlled foreign entities to engage in transactions, directly or indirectly, with the Government of Iran or any person subject to the jurisdiction of the Government of Iran that would otherwise be prohibited.
 - Did NOT authorize transactions involving:
 - Exportation, re-exportation, sale, or supply, directly or indirectly, from the U.S. of any goods, technology or services
 - Any transfer of funds to, from, or through a U.S. financial institution
 - SDNs
 - Any military, paramilitary, intelligence, or law enforcement entity of the Government of Iran, or any official, agent, or affiliate thereof
- **General License I** (issued on March 24, 2016): authorized U.S. persons to negotiate and enter into contingent contracts for the export of commercial aircraft and related parts and services to Iran.
- **Both were revoked on June 27, 2018**
 - OFAC included a wind down period for both
 - November 4, 2018 for General License H and August 6, 2018 for General License I

WITHDRAWAL FROM JCPOA

- President Trump announced on May 8, 2018, that the United States was withdrawing from the JCPOA.
- OFAC followed that announcement in June, 2018, by revoking several general authorizations that had been issued as part of the JCPOA (including General Licenses H and I) and amended the ITSR to implement wind-down periods for persons who had previously relied on the various general licenses.
- OFAC also issued guidance announcing its intention to re-impose the majority of secondary nuclear related sanctions and SDN designations that had been suspended under the JCPOA, subject to two separate wind-down periods of August 6, 2018 and November 4, 2018.
- On August 6, 2018, President Trump issued Executive Order 13846 formally re-imposing certain nuclear related sanctions with respect to Iran.
- The Blocking Statute was implemented the next day, on August 7, 2018.

EXECUTIVE ORDER 13846

- Issued on August 6, 2018 to formally re-impose, and in certain respects broaden, secondary sanctions that had been suspended pursuant to the JCPOA.
 - The intent was to capture all of the numerous sanctions authorities into one source.
- The order was consistent with the President's May 8, 2018 announcement regarding the withdrawal of the United States from the JCPOA.
- The order re-imposed secondary sanctions in accordance with the previously announced wind-down periods (August 6, 2018 and November 4, 2018).

EXECUTIVE ORDER 13846, CONT'D

- Broadened the scope of previously authorized sanctions by:
 - Providing new authority for imposing blocking sanctions on foreign persons for providing material support to other blocked persons.
 - Providing new authority for sanctions on foreign financial institutions that “knowingly conducted or facilitated any significant transaction” on behalf of a blocked person.
 - Broadening the menu of available sanctions to impose on persons who “knowingly” engage in certain significant transactions relating to Iranian petroleum, petroleum products, or petrochemicals.
 - Prohibiting non-U.S. entities owned or controlled by U.S. persons from engaging in transactions with certain blocked persons.

SECONDARY SANCTIONS EFFECTIVE AUGUST 7, 2018

- Effective August 7, 2018, secondary sanctions target non-U.S. persons that engage in transactions involving:
 - Purchase by Government of Iran: The purchase or acquisition of U.S. bank notes or precious metals by the Government of Iran.
 - Gold and Precious Metals: Iran's trade in gold or precious metals.
 - Raw Materials: The direct or indirect sale, supply, or transfer, to or from Iran, of graphite, raw or semi-finished materials such as aluminum and steel, coal, and software for integrating industrial processes.
 - Automotive Sector: The supply or financing of significant goods or services used in connection with Iran's automotive sector (including passenger cars, trucks, buses, and motorcycles).
 - Iranian Rials: Significant transactions related to the purchase or sale of Iranian rials, or the maintenance of significant funds or accounts outside the territory of Iran denominated in the Iranian rial.
 - Iranian Sovereign Debt: The purchase, subscription to, or facilitation of the issuance of Iranian sovereign debt.
 - Prohibited Parties: Transactions with individuals or entities that have committed serious human rights abuses, including censorship, against the people of Iran.

SECONDARY SANCTIONS EFFECTIVE NOVEMBER 5, 2018

- Effective November 5, 2018, secondary sanctions target non-U.S. persons that engage in the following activities:
 - Energy Sector: Transactions involving Iran’s energy sector, including the purchase, acquisition, sale, transport, or marketing of petroleum or petroleum products, or petrochemical products from Iran.
 - But see exceptions for countries that have significantly reduced their Iranian crude imports.
 - Shipping: Knowingly providing significant financial, material or other support to a person determined to operate a port in Iran or to be part of its energy, shipping and shipbuilding sectors.
 - the payment of routine fees and loading and unloading of cargo is allowed.
 - SDNs: Providing material support or assistance to, or goods or services in support of, the National Iranian Oil Company (“NIOC”), Nafitran Intertrade Company (“NICO”), and the National Iranian Tanker Company (NITC) or other SDNs in Iran.
 - Iranian Financial Institutions: Transactions by foreign financial institutions (FFIs) with the Central Bank of Iran (CBI) or designated Iranian financial institutions.
 - Insurance: The provision of related underwriting services, insurance, or reinsurance.

GENERAL LICENSES/WAIVERS THAT REMAIN

- Potential presidential waivers.
- Transactions related to Shah Deniz gas field.
- Agricultural commodities, medicine, and medical devices.
 - EAR99 and not on the List of Medical Devices Requiring Specific Authorization.
- Export of certain telecommunications goods and services.
- Temporary visits to Iran by U.S.-origin aircraft.

POTENTIAL SECONDARY SANCTIONS PENALTIES

- The potential penalties depend on the particular statute and provision under which it was issued. In general, three types of sanctions are authorized:
 - Blocking Sanctions: freezing the sanctioned entity's assets in the possession or control of US persons.
 - Restrictions on Accessing U.S. Financial System: prohibiting the opening, or imposing strict conditions on the maintaining, in the United States of a correspondent or payable through account.
 - Menu-Based: OFAC may choose from a number of different potential sanctions depending on the activity at issue. Examples include:
 - Denial of Ex-Im Bank loans
 - Prohibition on the export of U.S.-origin goods to the sanctioned entity
 - Prohibition on the import of goods, technology, or services into the United States from the sanctioned entity
 - Restrictions on access to U.S. government debt instruments
 - Prohibition on U.S. government procurement of any goods or services from the sanctioned entity
 - Denial of visas for executives from the sanctioned entity
 - Prohibition on certain loans from U.S. financial institutions
 - Prohibition on transactions in foreign exchange subject to jurisdiction of the United States
 - Prohibition on investing in or purchasing significant amounts of equity or debt instruments of the sanctioned entity

EU BLOCKING STATUTE (EC REGULATION 2271/96)

- The Blocking Statute came into force in 1996 in response to US extra-territorial sanctions relating to Cuba, Iran and Libya. On 7 August 2018, the Blocking Statute was updated to include the extra-territorial US sanctions on Iran that have or will be re-imposed as a result of the US withdrawing from the JCPOA.
- The EU has stated that *“the Blocking Statute aims to protect the established legal order, the interests of the Union and the interests of natural and legal persons exercising rights under the Treaty on the Functioning of the European Union against the unlawful effects of extra-territorial application of such legislation.”*
- The Blocking Statute’s main purpose is to protect EU operators engaging in lawful and international trade/movement of capital/related commerce activities with third countries pursuant to EU law. The basic principle is that EU operators shall not comply with the requirements or prohibitions identified in the specified US sanctions.
- **The Statute does NOT prohibit EU companies from withdrawing from the Iranian market due to independent financial or legal considerations.**

EUROPEAN BLOCKING STATUTE (EC REGULATION 2271/96)

- The European Union issued Commission Delegated Regulation 2018/1100 on June 6, 2018, updating the existing Blocking Statute (EC 2271/96). The Blocking Statute prohibits European “operators” from complying with US sanctions laws and regulations that are identified in the Annex to the Blocking Statute.
 - EU Operators includes: EU nationals who are residents in the EU; (2) any person in the EU acting in a professional capacity; and (3) any legal entity incorporated within the EU.
 - Branches of US companies in the EU are not subject to the Blocking Statute.
 - Subsidiaries of EU companies in the US are generally incorporated under the laws of the US and are therefore not subject to the Blocking Statute (but their parent companies are).
- U.S. sanctions identified in the Annex include: (1) the Iran Sanctions Act of 1996; (2) the Iran Freedom and Counter-Proliferation Act of 2012; (3) the National Defense Authorization Act for Fiscal Year 2012; (4) the Iran Threat Reduction and Syria Human Rights Act of 2012; and (5) the Iran Transactions and Sanctions Regulations.
 - These include the bulk of nuclear related sanctions that were re-imposed after the United States withdrew from the JCPOA. It does not, however, include sanctions issued, for example, under CAATSA or CISADA targeting the IRGC, Iran’s ballistic missile program, or its support for terrorism or human rights abuses.
- The European Union also published on August 7, 2018 related EU guidance.
- The updated Blocking Statute was effective as at August 7, 2018 and does not include any allowance for pre-existing contracts or agreements.

EUROPEAN BLOCKING STATUTE, CONT'D

- In particular, the Blocking Statute and related guidance:
 - Requires all EU operators to inform the European Commission (EC) within 30-days if their economic and/or financial interests are directly or indirectly impacted by the identified US sanctions.
 - Prohibits EU operators from complying, actively or by deliberate omission, with the requirements or prohibitions of the identified U.S. sanctions.
 - Provides for EU operators to request an authorization from the EC to comply with the identified U.S. sanctions.
 - Provides that EU operators may recover damages suffered as a result of the application of the identified U.S. sanctions.
 - Provides that any foreign judgment or administrative decision, including court rulings and arbitration awards, based on the identified U.S. sanctions is unenforceable in the EU.
 - States that seeking a U.S. license granting an exemption or derogation from the identified U.S. sanctions would be considered “compliance” with such US sanctions and, therefore, prohibited under the Blocking Statute. However, EU operators can request authorization from the EC to apply for a license in the US.
 - Speaking with U.S. authorities regarding the scope and impact of U.S. sanctions would not, however, be prohibited.

EU BLOCKING STATUTE – AUTHORIZATION TO COMPLY WITH US SANCTIONS

- Article 5 of the Blocking Statute provides for EU operators to request authorization from the EC to comply with US sanctions identified in the Annex if “non-compliance would ***seriously damage*** their interests or those of the Community.”
- The procedures for such a request are set forth in Articles 7 and 8. The European Commission also published a template for such requests along with an implementing regulation (2018/1101) setting forth assessment criteria to evaluate the requests. The criteria includes:
 - The relationship between the EU operator and the United States.
 - The existence of an ongoing administrative or judicial investigation against the applicant from, or a prior settlement agreement with, the United States.
 - Whether measures could be reasonably taken by the applicant to avoid or mitigate the damage.
 - The adverse effect on the conduct of the economic activity, in particular whether the applicant would face significant economic losses, which could, for example, threaten its viability or pose a serious risk of bankruptcy.
 - Whether the applicant’s activity would be rendered excessively difficult due to a loss of essential inputs or resources, which cannot be reasonably replaced.
- The applicant must detail the specific provisions of the U.S. sanctions that they would need to comply with and the precise activities that they would need to undertake. The burden is on the applicant to prove serious damage.
- There is no deadline by which the EC must process such requests other than a statement that applications will be handled as soon as possible.
- The applicant must comply with the Blocking Statute’s provisions while its application is pending.

EU BLOCKING STATUTE PENALTIES

- Each EU Member State is responsible for enforcing the Blocking Statute and determining the penalties for any violations of its terms. Penalties, therefore, will vary by Member State. The only common requirement is that penalties should be “effective, proportionate, and dissuasive.”
- Examples of member state penalties include:
 - Ireland, UK, Netherlands, Sweden: Criminal penalties.
 - *e.g.*, Ireland has a maximum penalty of 12 months imprisonment.
 - UK has a maximum penalty of an unlimited fine. There is also a possibility that a contractor may be debarred from public contracts if it has been convicted of a criminal offence.
 - Germany, Italy, Spain: Administrative penalties.
- France, Belgium, Luxembourg do not appear to have implemented the necessary laws to enforce the Blocking Statute.

EU BLOCKING STATUTE – POTENTIAL CIVIL DAMAGES

- Pursuant to Article 6 of the Blocking Statute, EU operators can recover *“any damages, including legal costs, caused to that person by the application of the laws specified in the Annex or by actions based thereon or resulting thereon.”*
- This provision has a broad application and damages can be claimed from not only responsible persons or entities, but also their representatives and intermediaries.
- Damages can take the form of seizure and sale of assets, which the person causing the damage holds in the EU, including shares that they may hold in companies incorporated within the EU.
- Members of a UK trade association called UK Finance have deemed the risk of civil litigation significant.

PRACTICAL CONSIDERATIONS

- **Evaluate Iran Business:** Consider whether Iran related business is worth maintaining.
 - For many EU companies, the limited nature of the Iranian market along with independent legal concerns (anti-money laundering, anti-bribery, financial, and litigation risk) have caused those companies to limit or exclude Iran from their business.
 - EU companies will find it increasingly difficult to carry on business in Iran, due to the number of companies that have already decided to exit the market. For example, companies in the supply chain may terminate their relationships, or banks may refuse to support transactions. According to the State Department, over 100 major international businesses have already announced an intent to leave Iran.
 - **If withdrawing from Iran due to business considerations, the rationale should be properly documented.**

PRACTICAL CONSIDERATIONS

- Consider whether the sanctions at issue are identified in the Annex to the Blocking Statute or other sanctions considerations that EU parties are permitted to comply with.
 - The annex, for example, does not include secondary sanctions issued under CAATSA or CISADA targeting the IRGC, Iran's ballistic missile program, human rights abuses or its support for terrorism.
 - Many secondary sanctions, moreover, have a dollar threshold or materiality requirement that should be considered.

PRACTICAL CONSIDERATIONS, CONT'D

- **Consider Licensing/Waiver Options:**

- Article 5 of the Blocking Statute provides for EU operators to request authorization from the EC to comply with the listed US sanctions.
- The Blocking Statute prohibits EU operators from seeking a license from OFAC requesting authorization to conduct activities prohibited by the listed US sanctions, without first obtaining an authorization from the EC to do so.
- Although potential waivers exist in most of the relevant sanctions programs, the United States has not shown an inclination to issue licenses or waivers to EU companies allowing them to continue operating in Iran.
 - The United States rejected a request from France, Germany, and the UK to waive enforcing US secondary sanctions on certain of their business sectors (*e.g.*, energy, automotive, civil aviation, and infrastructure) stating that the United States "*is not in a position to make exceptions to this policy except in very specific circumstances where it clearly benefits our national security [or humanitarian purposes].*"

PRACTICAL CONSIDERATIONS, CONT'D

- **Consider threat to bottom line posed by each set of regulations, including likelihood of enforcement.**
 - Small and medium sized companies will have different considerations than large multi-nationals.
 - Potential penalties under U.S. sanctions, particularly risk of being excluded from the U.S. market, are significant.
 - Penalties under the Blocking Statute are more varied.
 - Likelihood of enforcement is unclear and will depend to a large extent on political considerations.
 - Many EU Member States such as Belgium, France and Luxembourg currently lack the necessary laws to even enforce violations of the Blocking Statute.
 - Despite being in force for over 20 years, there have been no reported civil or criminal penalties levied in an EU Member State based on the Blocking Statute.
 - We cannot assume it will continue to be limited going forward.

PRACTICAL CONSIDERATIONS, CONT'D

- There have been examples of EU Member States investigating potential breaches of the Blocking Statute.
- Also remember potential of private action under Article 6.
 - *e.g.*, multinational company pulls out of an Iran project because of U.S. sanctions and voids contracts with service or parts providers. Under the Blocking Statute, those service and parts providers could now sue and claim damages against the multinational. Similar issues could exist for financial institutions that refuse to do business in the EU with parties that are prohibited under US law but not under the EU sanctions regime.
- Although U.S. secondary sanctions have, similarly, only been imposed sparingly, the new administration has suggested it will pursue strict enforcement of these sanctions. Whether it will do so remains to be seen.

PRACTICAL CONSIDERATIONS, CONT'D

- **“Foreign Sovereign Compulsion Defense”**

- Under the foreign state compulsion doctrine, a country is not to punish a person from taking action in another country that is required by the laws of that country.
- Rejected by OFAC in the past.
 - *e.g.*, Cuban Pajamas
- Some U.S. courts have held that a party should not be criminally or civilly liable under U.S. law for activity in a foreign country that is compulsory under the laws of that country. However, others have discounted its applicability, at least in the criminal context.
 - *e.g.*, Bro-Tech Corporation
- Dearth of prosecutions also suggests a fair amount of prosecutorial restraint.
- Prosecution under blocking statutes is even more rare as it is difficult to obtain evidence of a company’s intent in not doing something.

PRACTICAL CONSIDERATIONS , CONT'D

- **Payment for Lawful Transactions**

- Many international banks have been refusing to process financial transactions involving Iran, even if not technically prohibited under the various US or EU sanctions regulations.
 - European Investment Bank – President of the European Investment Bank (an institution owned by the EU Member States), despite pressure from the EU, has publicly stated that the institution's global operations would be put at risk if it continued its Iranian activities in light of U.S. sanctions and confirmed that the bank will not operate in Iran.
 - German Bundesbank – Revised its terms and conditions on cash withdraws applicable to German financial institutions to include a provision that allows the banks to reject certain requests from Iran which would "threaten the banks relationships with other central banks or financial institutions."
- SWIFT may, as it was forced to do in 2012, be required to disconnect Iranian financial institutions from its network.
 - As part of the JCPOA, many Iranian banks were able to reconnect with SWIFT.
- France, Germany, and the UK are considering developing an independent EU payment system but the precise nature of the system, and any US response, are still undeclared.

PRACTICAL CONSIDERATIONS, CONT'D

- **Contractual Terms**

- Be careful of the terminology used in contractual clauses: *Mamancochet Mining Ltd v Aegis Managing Agency Ltd & Others*.

- **Avoid U.S. nexus**

- Payment in currency other than dollars (beware crypto-currencies).
- Non-U.S.-origin goods and technology.
- Screen for SDNs.

- **Legal Challenges to U.S. Sanctions**

- ICJ opinion.

- **Mid-Term Elections Pending in the U.S.**

- **Brexit**

- All UN and EU sanctions are currently implemented by EU Regulations, which are directly applicable on the UK. This will change post Brexit.
- The terms of any agreement regarding the UK's post Brexit involvement in EU foreign policy, including sanctions, remains unclear. However, the UK is strongly opposed to the US decision to leave the JCPOA and therefore it is likely to remain fully aligned with the EU on this issue post Brexit.

Biography



Stefan Reisinger

Of Counsel

Washington, D.C.

stefan.reisinger@morganlewis.com

+1.202.739.5102

[Click here for full biography](#)

Stefan has more than 15 years of experience advising clients on United States and multilateral export, economic sanctions, anticorruption, and customs matters. His practice covers all aspects of these areas, including counseling, training, licensing, opinion work, compliance audits, internal investigations, responding to government enforcement actions, and developing and implementing relevant compliance policies and procedures. Stefan has led comprehensive, worldwide, investigations and audits and responded to enforcement actions involving multiple jurisdictions and government agencies.

Biography



Nicola Kelly

Associate
London

nicola.kelly@morganlewis.com

+1.202.739.5102

[Click here for full biography](#)

Nicola represents corporate entities, senior executives, and employees in connection with commercial and international dispute resolution, cross-border internal investigations, regulatory investigations and enforcement proceedings, criminal prosecutions, and civil proceedings. She has advised clients on complex regulations and investigations concerning UK, EU, and international sanctions and export controls, as well as representing clients in cross-border civil proceedings in the English Courts.

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