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## President Obama Signs New Iran Sanctions into Law

On July 1, 2010, President Obama signed the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (the “Act”) into law. The Act substantially increases both the activities that may lead to sanctions on U.S. and foreign persons who deal with Iran and the potential severity of those sanctions, although it maintains the basic structure of the prior law pursuant to which most sanctions are not automatic but require further action by the executive branch. Of particular note, the Act:

- expands existing sanctionable activities for foreign companies involving “investment” in the Iranian petroleum industry to include selling, purchasing, or financing goods, services, or technology in connection with such investments;
- adds new sanctionable activities for foreign companies, including providing refined petroleum products to Iran, providing goods, services, technology, or support to the maintenance or expansion of Iranian refining capacity, or providing goods, services, technology, or support (explicitly including insurance, financing, or shipping) that contribute to Iran’s ability to import refined products;
- expands the potential (but not mandatory) penalties for foreign persons engaged in sanctionable activities to include comprehensive U.S. economic sanctions and asset freezes, makes investigations of suspected violations mandatory, extends sanctions to parent entities that knew or should have known of their subsidiaries’ sanctionable activities, and raises the barriers to granting waivers to entities found to have engaged in sanctionable activity;
- adds a number of provisions affecting U.S. and foreign financial institutions, including:
  - potential sanctions for financing investments in the Iranian petroleum or refining sectors or financing the import of refined products, as described above;
  - denial of U.S. correspondent accounts to foreign financial institutions found by the U.S. government to have facilitated transactions for U.S.-designated parties linked to the Iranian Revolutionary Guards or Iranian weapons of mass destruction (“WMD”) or terror activities;

- requirements for the Treasury Department to adopt regulations imposing due diligence requirements on U.S. banks to ensure that they are not providing correspondent services to institutions engaged in activities described in the previous point;
- extension of OFAC compliance requirements with respect to Specially Designated Nationals connected to the Iranian Revolutionary Guards to foreign subsidiaries of U.S. financial institutions;
- bars from U.S. government procurement entities that have engaged in sanctionable activities in the Iranian petroleum or refining sectors or that have provided equipment to Iran used in monitoring or disrupting communications;
- rescinds limited exceptions to current sanctions, thus barring virtually all U.S. exports and imports to and from Iran; and
- authorizes state and local divestment legislation with respect to companies involved in the Iranian petroleum sector.

A more detailed description of the Act follows.

## **I. Amendments to the Iran Sanctions Act**

### **A. Restricted Activity**

The Act adds new categories of activity sanctionable under the ISA. Foreign persons and entities may become subject to such sanctions if they knowingly:

- Provide goods, services, technology, information, or support to Iran, or enter into any contract to do so, that “could directly and significantly facilitate” the maintenance or expansion of Iran’s domestic production of refined petroleum products;<sup>1</sup> or
- Provide Iran with refined petroleum products, or providing any goods, services, technology, or support that “could directly and significantly contribute” to Iran’s ability to import refined petroleum products (specifically including financing,

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<sup>1</sup> Includes diesel, gasoline, jet fuel (including naphtha-type and kerosene-type jet fuel), and aviation gasoline. Act § 102(f)(7).

brokering, insurance, or shipping services relating to any such goods, services, technology, or support).<sup>2</sup>

In each case, the activity is sanctionable if the value of the relevant transaction exceeds \$1,000,000 for any one transaction or \$5,000,000 in aggregate over a one-year period.

The Act also broadens the scope of sanctionable activity under the prior ISA regime. Under the existing ISA, parties that make an “investment” of \$20 million or more (provided that only individual investments of \$5 million or more are counted toward the \$20 million total) in any twelve-month period that contribute to Iran’s ability to develop “petroleum resources” are eligible for sanctions. The Act retains this criterion but substantially expands the definition of “investment”<sup>3</sup> and also expands the definition of “petroleum resources.”<sup>4</sup>

The definition of “investment” was significantly expanded by deleting the prior exclusion for “the entry into, performance, or financing of a contract to sell or purchase goods, services, or technology.”<sup>5</sup> The conference report accompanying the legislation confirms that the deletion was intended to expand the definition of “investment” to include these activities.<sup>6</sup> Thus, activities that historically have not been, and ordinarily would not be, considered direct investment in Iran’s petroleum sector, such as financing the supply of equipment to an Iranian oil company, now are potentially sanctionable.

Moreover, the Act redefines “knowingly” to include persons that “should have known” about sanctionable activity in which they engaged, whereas the prior ISA required persons to have “actual knowledge” of such activity to be eligible for sanctions.<sup>7</sup>

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<sup>2</sup> The Act creates an exception for underwriters and insurers if they exercise due diligence in creating and enforcing policies and procedures to ensure the prevention of offering such services previously described. *Id.* § 102(a).

<sup>3</sup> Under the prior ISA and the Act, “investment” includes not only equity and royalty arrangements (including additions to existing investment) but also any contract that includes “responsibility for the development of petroleum resources” of Iran, interpreted to include pipelines to or through Iran. However, the prior definition of “investment” excluded “the entry into, performance, or financing of a contract to sell or purchase goods, services, or technology.” The Act deletes this exception. *Id.* § 102(f)(2).

<sup>4</sup> The prior definition “includes petroleum and natural gas resources.” The Act expands this definition to include “petroleum, refined petroleum products, oil or liquefied natural gas, natural gas resources, oil or liquefied natural gas tankers, and products used to construct or maintain pipelines used to transport oil or liquefied natural gas.” *Id.* § 102(f)(6).

<sup>5</sup> *Id.* § 102(f)(6).

<sup>6</sup> COMM. OF CONFERENCE FOR H.R. 2194, 111<sup>TH</sup> CONG., JOINT EXPLANATORY STATEMENT OF THE COMM. OF CONFERENCE 15 (Comm. Print. 2010).

<sup>7</sup> Act § 102(f)(4).

Also, the Act provides that entities that own or control persons engaged in sanctionable activities are themselves subject to sanctions if they “had actual knowledge or should have known” of their subsidiaries’ activities.<sup>8</sup>

## B Available Sanctions

The prior ISA required the President to impose any two sanctions out of a menu of six against persons who invested \$20 million or more in Iran’s petroleum sector in any 12-month period.<sup>9</sup> The Act adds three new sanctions to this menu (the “New Sanctions”), expanding the menu to nine, and requires the President to impose three sanctions from the expanded menu against persons determined to have engaged in any sanctionable activity related to investment in the petroleum sector or provision of refined petroleum products described in Part A, above. The New Sanctions allow the President to prohibit any person subject to the jurisdiction of the United States from engaging in:

- Foreign exchange transactions in which the sanctioned person has any interest;
- Financial transactions involving the sanctioned person; and/or
- Transactions or dealings involving the “property” of the sanctioned person.

These sanctions, if applied, would essentially subject the sanctioned person to full OFAC sanctions and would effectively cut them off from U.S. investors, the U.S. financial system, and the U.S. markets. However, unlike earlier versions of the legislation, the final Act does not make these enhanced sanctions mandatory.

## C. Investigations and Waiver Authority

It remains the case that the imposition of the sanctions described above is not automatic upon engaging in sanctionable activity. A person engaged in sanctionable activity will only be subject to sanctions following an investigation and order imposing sanctions under the authority of the President. However, the Act contains a number of provisions designed to increase the likelihood that sanctions will actually be imposed.

The Act changes the recommendation that the President “should” investigate potentially sanctionable activities to a requirement that the President “shall” investigate such activities.<sup>10</sup> It also requires the President to determine whether such investigated activity is sanctionable under the Act within 180 days. Both such processes were discretionary under

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<sup>8</sup> *Id.* § 102(a)(3)(B).

<sup>9</sup> ISA § 5(a).

<sup>10</sup> Act § 102(g)(5)(A).

the prior ISA. Although there is no mechanism to enforce the new requirement that the President conduct investigations and issue findings, there are enhanced requirements to make reports to Congress that are designed to increase pressure to do so.

However, the Act affords the President discretion to:

- cease an investigation if the President certifies that the investigated person is no longer engaging in the sanctionable activities and has received reliable assurances that the person will refrain from engaging in such activities in the future;<sup>11</sup>
- issue waivers of sanctions if the President finds such a waiver to be “necessary to the national interest” (formerly “important to the national interest”);<sup>12</sup>
- delay the investigative requirement to investigate potentially sanctionable activity concerning refined petroleum products if the President certifies that there was a substantial aggregate reduction in such activities for the year following the Act’s enactment (such delays may be repeated indefinitely);<sup>13</sup> and
- issue a 12-month waiver of sanctions against a person if the government with jurisdiction over that person is closely cooperating in multilateral efforts to control the proliferation of WMD and advanced conventional weapons to Iran and the waiver is vital to national security interests.<sup>14</sup>

#### D. Government Procurement

The Act contains two sets of mandatory sanctions related to U.S. government procurement. First, every U.S. government contractor will be required to certify that it has not engaged in any sanctionable activities related to the Iranian petroleum or refined product sectors (whether or not sanctions have in fact been imposed); any entity making a false certification will be subject to termination of the contract or debarment from government contracting.<sup>15</sup> This requirement commences with solicitations for contracts issued on or after the date that is 90 days from the date of enactment of the Act.

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<sup>11</sup> *Id.* § 102(g)(5)(C).

<sup>12</sup> *Id.* § 102(c)(2)(B). Waivers granted under the prior ISA remain valid under the Act. *Id.* § 102(h)(6).

<sup>13</sup> *Id.* § 102(h)(4)(B).

<sup>14</sup> *Id.* § 102(g)(2)(A).

<sup>15</sup> *Id.* § 102(b)(3).

Second, the Act contains a new set of penalties for companies that export hardware, software, or other telecommunications equipment that the President determines is to be used specifically to restrict the flow of information in Iran or to disrupt, monitor, or otherwise restrict communications. Any entity supplying such equipment is to be barred from U.S. government contracts.<sup>16</sup>

## **II. Provisions Applicable to Financial Institutions**

In addition to the provisions above making financing of imports to Iran of refined products or of investments in the Iranian petroleum sector sanctionable, there are a number of other provisions relevant to financial institutions.

The Act requires the Secretary of the Treasury (the “Secretary”) to issue regulations prohibiting or strictly controlling opening or maintaining a correspondent account or a payable-through account in the United States for a foreign financial institution that facilitates:

- Iran’s efforts to acquire WMD;
- Iran’s support of foreign terrorist groups;
- the activities of a person subject to relevant United Nations Security Council (“UNSC”) resolution sanctions; or
- any significant transaction supporting the Iranian Revolutionary Guard Corps (“IRGC”), an entity designated under OFAC sanctions as an affiliate of the IRGC, or a financial institution whose property is blocked under OFAC sanctions due to WMD- or terrorism-related activities.<sup>17</sup>

With respect to U.S. financial institutions, the Act extends OFAC prohibitions against dealing with Specially Designated Nationals linked to the IRGC to any person owned or controlled by a domestic financial institution.<sup>18</sup> The Act also contains requirements, modeled on the USA PATRIOT Act, requiring the Department of the Treasury to issue rules obligating domestic financial institutions to conduct due diligence on their correspondents to help ensure that they are not engaged in sanctionable acts.<sup>19</sup> The Act

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<sup>16</sup> *Id.* § 106.

<sup>17</sup> *Id.* § 104(c).

<sup>18</sup> *Id.* § 104(d).

<sup>19</sup> *Id.* § 104(e).

does not specify the precise content of the regulations, and it remains to be seen what detailed requirements will be imposed.<sup>20</sup>

### III. Divestment Initiatives

The Act authorizes—but does not require—state and local governments to adopt laws requiring government entities under their control to divest investments in firms having at least a \$20 million investment in the Iranian energy sector.<sup>21</sup> The Act clarifies that prior divestment laws that do not meet the new thresholds for an Iran-related divestment law are “grandfathered” in. The Act also shields investment companies and their officers, directors, employees and advisors from criminal, civil, and administrative liability based on such divestment, and expresses Congress’s sense that divestment from or avoidance of investment in Iran breaches no fiduciary duty under the Employee Retirement Income Security Act (“ERISA”).<sup>22</sup>

### IV. Export Controls

The Act requires the President to designate a country as a “Destination of Diversion Concern” if the President determines that such country allows substantial diversion of goods, technology, and services that could be used in WMD programs or for the support of terrorism to Iranian end-users.<sup>23</sup> Following such a designation, exports to that country of goods found to be subject to diversion must be subject to license requirements, with a presumption that licenses will be denied. However, the President may delay imposition of the licensing requirements if he finds that the country is taking steps to impose effective export controls.

The Act also rescinds the limited authorizations to import Iranian goods to the United States that exist under current law. Substantially all imports and exports of goods, services, and technology between the United States and Iran are now prohibited.<sup>24</sup>

Finally, if any person is penalized under the existing sanctions relating to the transfer of nuclear technology to Iran, the Act requires the suspension of nuclear technology transfers to the country with jurisdiction over that person. Technology transfers may be

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<sup>20</sup> The Act explicitly leaves “foreign financial institution” and “domestic financial institution” open for definition by regulation. *Id.*

<sup>21</sup> *Id.* § 202.

<sup>22</sup> *Id.* §§ 203-4.

<sup>23</sup> *Id.* § 303.

<sup>24</sup> *Id.* § 103(b).

permitted if the President determines that the country in question was unaware of or is taking action against such transfers, or individual transfers may be licensed if vital to the national interest.<sup>25</sup>

**V. Other Provisions**

Other provisions of the Act include:

- visa, property, and financial sanctions on Iranian officials and their agents who committed serious human rights abuses against Iranian citizens following the June 12, 2009 Iranian Presidential elections;<sup>26</sup>
- authorization for the President to prescribe regulations for implementing Iran-related UNSC resolutions;<sup>27</sup> and
- harmonization of maximum criminal penalties under various U.S. economic sanctions statutes at 20 years' imprisonment and a \$1 million fine.<sup>28</sup>

The effective date of the operative provisions of the Act is, except as noted, is generally the date of enactment (July 1, 2010). Petroleum-related investments commenced before that date will be subject to the substantive provisions of the prior act; however, the mandatory investigation provisions will apply to investments commenced prior to the date of enactment but continued afterwards, and the full range of enhanced sanctions will apply to WMD-related activities that continue following the date of enactment.<sup>29</sup>

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<sup>25</sup> *Id.* § 102(a)(2)(D).

<sup>26</sup> *Id.* § 105.

<sup>27</sup> *Id.* § 108.

<sup>28</sup> *Id.* § 107.

<sup>29</sup> *Id.* § 102(h).



If you have any questions regarding the foregoing or other sanctions matters, please feel free to speak with your regular contacts at the firm or any of the following:

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