

To: Our Clients and Friends

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New Sanctions Against Iran Highlight Critical Change in U.S. Sanctions Policy

New sanctions recently have been levied against Iran by the U.S. Government that will significantly impact non-U.S. subsidiaries of U.S. companies that currently have business directly or indirectly with or involving Iran. On August 10, 2012, the President signed The Iran Threat Reduction and Syria Human Rights Act of 2012, H.R.1905 (“the Act”) (P.L. No. 112-158). Notably, Section 218 of the Act requires the President to issue an executive order to prohibit entities owned or controlled by a U.S. person, such as a non-U.S. incorporated subsidiary of a U.S. parent company, from engaging in any dealings or transactions with Iran that if undertaken in the U.S. or by a U.S. person, would violate U.S. sanctions law. The President must issue the executive order no later than October 9, 2012. Section 218 also makes the U.S. parent company liable for violations committed by its overseas entities. While the President has not yet issued an executive order imposing the restrictions on such non-U.S. entities, entities that will be affected by the new executive order should take immediate steps to ensure compliance.

The Act is but one of myriad measures taken recently by the U.S. Government to tighten sanctions against Iran by the U.S. Government. In the past several months, the U.S. Government has strengthened restrictions on foreign sanction evaders, human rights abusers using information technology, and additional persons involved with Iran’s nuclear program.

Overview of Current Restrictions

Currently, with certain exceptions principally dealing with transfers to Iran of U.S. origin items or non-U.S. items containing certain U.S. origin content, subsidiaries and affiliates of U.S. companies that are separately incorporated overseas generally are not required to comply with U.S. sanctions against Iran set forth in the Iranian Transactions Regulations (“ITR”). U.S. law does allow the U.S. Government to sanction non-U.S. entities for engaging in certain activities relating for example to Iran’s petroleum and nuclear industries and its efforts to procure weapons of mass destruction or provide support to terrorist organizations or for terrorism activities.

U.S. persons (i.e., U.S. companies and their non-U.S. branches, U.S. citizens/permanent residents, and anyone located in the United States) are required to comply with the sanctions imposed under the ITR. Specifically, U.S. persons are prohibited from engaging in most dealings directly or indirectly with Iran:

- The export, reexport, sale, or supply, directly or indirectly, of any goods, technology, or services to Iran or the Government of Iran (including entities owned or controlled by the Government of Iran, wherever located), or to entities that will ultimately supply the products to those entities. This prohibition includes the provision of financial services as well as any other service, such as administrative support, IT support, or other general services;
- Imports into the United States from Iran or of Iranian-origin goods;

- Trade related transactions with Iran, including any transactions or dealings related to (i) goods or services of Iranian origin or owned and controlled by the Government of Iran, or (ii) goods, technology, or services for exportation, reexportation, sale or supply, directly or indirectly, to Iran or the Government of Iran;
- Investments in Iran;
- Facilitation of transactions involving Iran, including approving, financing, or undertaking actions to support a transaction with Iran. Examples of facilitation include referral of business or a business opportunity overseas, administrative support services or any other assistance in connection with a targeted country, government or person, financing or guaranteeing a transaction, or altering internal policies or procedures to allow a foreign person to perform a transaction; and
- Evasion and attempts or conspiracy to evade U.S. sanctions.

Current law also requires U.S. persons to block (or “freeze”) any assets of the Government of Iran, Iranian persons (such as Iranian banks and the Islamic Republic of Iran Shipping Lines) designated on the List of Specially Designated Nationals and Blocked Persons (the “SDN List”) or entities located anywhere that are owned or controlled by the Government of Iran or designated Iranian persons that come into the U.S. person’s possession or control.

In certain instances, foreign policy interests favor the issuance of licenses to U.S. persons to authorize specific dealings with Iran that otherwise would be prohibited under the sanctions laws. For example, the Trade Sanctions Reform and Export Enhancement Act of 2000 (“TSRA”) allows exports and certain reexports of agricultural commodities, medicines and medical devices to Iran, provided that the U.S. person obtains a license from the U.S. Department of the Treasury, Office of Foreign Assets Control (“OFAC”).

New Sanctions Prohibit Dealings by Non-U.S. Entities

Upon issuance of the Presidential executive order, non-U.S. entities that are owned or controlled by a U.S. person will be prohibited from engaging in activities where the U.S. person is prohibited from engaging in such activities under U.S. law. Non-U.S. entities that will be considered to be “owned or controlled” by a U.S. person, and therefore must comply with U.S. sanctions against Iran, are those entities in which a U.S. person holds more than fifty percent equity interest by vote or value, or a majority of the seats on the board of directors of the entity, or in which a U.S. person otherwise controls the actions, policies, or personnel decisions of the entity.

The Act requires that, upon issuance of the executive order, all activities described above will be prohibited, including but not limited to transfers to Iran or the Government of Iran of U.S. origin items classified as EAR99 supplied from overseas inventories and the supply of non-U.S. origin items and services. In addition, the Act also appears to extend restrictions under the U.S. Export Administration Regulations (“EAR”) to non-U.S. entities that are owned or controlled by a U.S. person. Currently, the EAR prohibit U.S. persons engaging in unlicensed activities related to the proliferation of nuclear explosive devices, chemical or biological weapons, missile technology, and proliferation of chemical weapons. As required by the Act, the executive order will prohibit non-U.S. entities that are owned or controlled by a U.S. person from performing any contract, service, or employment that it knows or has reason to know will directly assist in the design, development, production, stockpiling, or use of chemical or biological weapons in or by Iran.

The Act does not contain contract sanctity or other provisions that would allow for a transition period during which the non-U.S. entity owned or controlled by a U.S. person is permitted to terminate or wind down business, transactions or other dealings with or related to anyone subject to the

jurisdiction of the Iranian Government, the Government of Iran or entities owned or controlled by the Government of Iran. Last year, in connection with the expansion of sanctions against Syria, OFAC did issue a general license authorizing U.S. persons to wind down operations with Syria; however, it remains to be seen whether the executive order implementing these new prohibitions affecting Iran or any subsequent general licenses from OFAC will authorize wind-down transactions.

At this time, it is also not clear whether current licensing policies, including those applicable to TSRA, will apply to non-U.S. subsidiaries. The Act requires that the prohibitions under current law be extended to non-U.S. entities owned or controlled by a U.S. person. It is silent with respect to whether the non-U.S. entity will be subject to the same licensing policies as its U.S. parent.

Finally, while the Act does not appear to require the President to extend the blocking requirements to non-U.S. persons, non-U.S. entities owned or controlled by a U.S. person will be prohibited from dealing in or with property of the Government of Iran, persons subject to the jurisdiction of the Iranian Government designated on the SDN List, or persons owned or controlled by the Government of Iran or such designated persons, regardless of whether the non-U.S. entity is required to block such property. Moreover, should any property in which the Government of Iran, an Iranian person designated on the SDN List or any entity owned or controlled by the Government of Iran or a designated Iranian person, such as funds, a contract, an account, etc., come into the possession or control of a U.S. parent company or another U.S. person, the U.S. parent or U.S. person would be required to block the property. Following issuance of the executive order, U.S. parent companies will need to remain cognizant of their own obligations to comply with U.S. sanctions provisions, including the ITR, as well as the blocking requirements in connection with any termination of contracts or wind-down activities by their non-U.S. subsidiaries.

U.S. Parent Company Liability for Violations by Its Non-U.S. Subsidiaries

The Act specifically imposes civil liability on U.S. persons for violations committed by their overseas entities. Potential penalties for such violations include civil fines up to the greater of \$250,000 per violation or twice the amount of the transaction. Non-U.S. entities also may be subject to penalties or sanctions for their own activities under the ITR and other U.S. laws.

The Act allows a U.S. parent company or other U.S. person to escape liability for violations by its non-U.S. subsidiary only if the U.S. person divests or terminates its business with its non-U.S. subsidiary within 180 days after the date of the enactment of the Act. Such divestment or termination must occur by February 6, 2013. As noted above, there is no provision that allows the non-U.S. subsidiary the sort of “winding down” of business activities associated with completing the servicing of a contract or return of an advance payment nor does it permit, for example, the non-U.S. entity to receive payment from the Iranian person on a contract for products or services that the non-U.S. entity may have already rendered prior to issuance of the executive order.

Thus, to the extent that a non-U.S. subsidiary owned or controlled by a U.S. parent is engaged in business with Iran or the Government of Iran as of the date the President issues an executive order extending the sanctions against Iran and that non-U.S. subsidiary does not have authorization to engage in such activities, its U.S. parent could be held liable unless the U.S. parent takes action by February 6, 2013 to terminate its relationship with or divest the non-U.S. subsidiary. Potentially, it will not be sufficient for the non-U.S. subsidiary to terminate its activities with Iran after the executive order takes effect (unless wind-down or other authorization is provided or obtained).

Additional Sanctions

The Act further expands existing sanctions law with respect to Iran in the following ways:

- Requires publicly traded companies listed on the New York Stock Exchange or the NASDAQ to disclose in quarterly and annual reports information regarding dealings by the reporting entity or any of its affiliates with designated purveyors of weapons of mass destruction, terrorists, or the Government of Iran, and where such dealings have occurred, requires that the President initiate an investigation.
- Expands sanctions against persons who provide support to Iran's energy sector, including participation in certain petroleum resources development joint ventures located anywhere in the world in which the Government of Iran is a substantial partner or investor, or through which Iran could otherwise receive energy sector technology or know-how not previously available to its Government and the provision of goods and services, including shipping services, to Iran's energy sector.
- Requires the blocking of assets of, and imposes other sanctions on, persons that knowingly provide ships, insurance or reinsurance, or other shipping services, for transportation of goods that materially contribute to Iran's proliferation of weapons of mass destruction or terrorism-related activities. The sanctions apply to U.S. parents companies that knew or should have known of the sanctionable activity and to any of their subsidiaries or affiliates that knowingly participated in the activity.
- Imposes new sanction with respect to persons who engage in censorship or other related activities against citizens of Iran. This includes satellite service providers and other entities that have direct contractual arrangements to provide satellite services to the Government of Iran or entities that are owned and controlled by the Government of Iran.
- Extends U.S. financial sanctions imposed on entities identified in United Nations Security Council resolutions to persons acting on behalf of, at the direction of, or owned or controlled by, the designated entities.
- Imposes new sanctions on the Iran Revolutionary Guard Corps Officials, its agents and affiliates.
- Authorizes the exclusion from the United States of aliens who are corporate officers, principals or controlling shareholders in a sanctioned firm, and places new immigration restrictions on senior Iranian officials and their family members.

Conclusion

The new Act and the forthcoming executive order will more closely align the ITR with the U.S. sanctions currently in place against Cuba. No longer will non-U.S. foreign affiliates or subsidiaries of a U.S. company be able to merely comply with their own country's local law with respect to transactions involving Iran. This new law solidifies the extraterritorial reach of U.S. sanctions as applied to a U.S. company's overseas operations relating to Iran. Companies have a limited time to address the forthcoming changes to their international operations.

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