New Executive Order Re-Imposing U.S. Sanctions Against Iran and Entry Into Force of Updated EU Blocking Statute

August 8, 2018

International Trade Controls

On August 6, 2018, President Trump issued Executive Order 13846 (the "Executive Order") that re-imposes -- and to a limited extent broadens the scope of -- certain U.S. secondary sanctions targeting Iran that had been suspended in January 2016 pursuant to the Joint Comprehensive Plan of Action ("JCPOA") with Iran. The Trump Administration had previously announced that these sanctions would snap back into force in two phases in connection with the U.S. withdrawal from the Iran nuclear deal.

The issuance of the Executive Order coincides with the end of the 90-day wind-down period on August 6 for activities covered by an initial set of U.S. secondary sanctions that had been suspended under the JCPOA; the 180-day wind-down period for activities covered by the second set of secondary sanctions will expire on November 4.

In connection with these developments, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") has published new Frequently Asked Question ("FAQ") guidance regarding the purpose, scope, and implementation of the Executive Order, and has also updated existing FAQ guidance regarding the Iran sanctions snap-back and relevant wind-down periods.

Coinciding with these U.S. sanctions developments, the updated EU Blocking Statute also came into force on August 7, 2018 (European Council Regulation No. 2271/96, as amended here). The European Union along with the foreign ministers of France, Germany and Britain also issued a joint statement expressing determination to "protect European economic operators engaged in legitimate business with Iran, in accordance with EU law and with UN Security Council resolution 2231" on the Iran nuclear deal.

Iran-Related Executive Order

The Obama Administration had implemented the sanctions relief contemplated by the JCPOA both by revoking or amending certain pre-JCPOA executive orders sanctioning Iran, and by waiving certain sanctions imposed by U.S. federal statutes pursuant to authorities in those statutes. The Executive Order re-imposes relevant provisions of the pre-JCPOA executive orders that were revoked or amended as part of the JCPOA implementation. The secondary sanctions re-imposed by the Executive Order target primarily non-U.S. persons that engage in certain dealings with Iran, and the order re-imposes these measures in accordance with the previously announced wind-down periods for the sanctions snap-back.

In parallel with the Executive Order, the Trump Administration is re-imposing other Iran-related sanctions codified in federal statutes by revoking waivers of those sanctions.

Sanctions Re-Imposed on August 7, 2018

As expected, the Executive Order -- along with actions taken by the Trump Administration to revoke statutory sanctions waivers -- re-impose, as of August 7, 2018, secondary sanctions targeting non-U.S. persons that engage in dealings with Iran in the following areas:

- The Government of Iran's purchase or acquisition of U.S. bank notes or precious metals;
- Iran's trade in gold or precious metals;
- 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;
- Iran's automotive sector;
- 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; and
- The purchase, subscription to, or facilitation of the issuance of Iranian sovereign debt.

In addition, certain wind-down general licenses previously issued by OFAC expired on August 6. These authorizations had temporarily permitted the wind-down of transactions that were previously authorized under general licenses issued by OFAC in connection with the JCPOA and revoked on June 27, 2018.

Sanctions to be Re-Imposed on November 5, 2018

As outlined in our prior alert dated May 9, 2018, additional secondary sanctions will be re-imposed following the 180-day wind-down period ending on November 4, 2018, including a range of measures targeting Iran's energy, financial, shipping, and insurance sectors. The Executive Order provides the foundation for these additional secondary sanctions as well.

Expanded Scope of Sanctions

While the Executive Order largely re-imposes pre-JCPOA sanctions, as detailed in new OFAC FAQ 601, the Executive Order also broadens the scope of the sanctions by:

- Providing new authority for imposing blocking sanctions on any person determined, on or after November 5, 2018, to have provided "material support for, or good or services in support of," persons separately blocked pursuant to other provisions of the Executive Order and relevant statutory sanctions authorities;
- Providing new authority for sanctions relating to correspondent and payable-through accounts of foreign financial institutions determined to have, on or after November 5, 2018, "knowingly conducted or facilitated any significant transaction on behalf of" certain persons blocked pursuant to the Executive Order;

- Broadening the menu of available sanctions to impose on persons determined to have, on or after November 5, 2018, knowingly engaged in certain significant transactions relating to Iranian petroleum, petroleum products, or petrochemicals, to include, for instance, measures targeting corporate officers, principals, or controlling shareholders of the sanctioned party; and
- Prohibiting non-U.S. entities owned or controlled by U.S. persons from engaging in transactions with certain blocked persons, including (1) persons blocked for providing material support for, or goods and services in support of, Iranian persons on OFAC's List of Specially Designated Nationals and Blocked Persons ("SDN List") and certain other designated persons; and (2) persons blocked for being either part of the Iranian energy, shipping, or shipbuilding sectors or a port operator in Iran, or for knowingly providing significant support for certain other blocked parties.

These relatively minor changes to the scope of the sanctions that were in effect prior to the JCPOA are intended to provide for greater consistency in the U.S. government's administration of the sanctions. They are unlikely to impact significantly the sanctions exposure of U.S. or non-U.S. persons.

Scope of Permissible Wind-Down Activities

OFAC's updated FAQ guidance also provides additional clarification regarding the scope and extent of permissible wind-down activities in connection with the re-imposition of the Iran sanctions.

Non-U.S., Non-Iranian Persons

As described in our May 9 alert, OFAC previously advised that non-U.S., non-Iranian persons may, under certain conditions, receive payments after the end of the applicable 90-day or 180-day wind-down period for goods or services "fully provided or delivered to an Iranian counterparty" prior to the end of the applicable wind-down period, without facing exposure to secondary sanctions. OFAC's new FAQ guidance clarifies that this allowance applies if all of the following conditions are met:

- The transaction occurred pursuant to a written contract or agreement entered into prior to the May 8, 2018 announcement of the U.S. withdrawal from the JCPOA;
- The relevant activities were consistent with U.S. sanctions in effect at the time of delivery or provision of the relevant goods or services, and did not involve persons on the SDN List at the time of the transactions; and
- Any payments are consistent with U.S. sanctions, including by not involving any U.S. persons or the U.S. financial system.

OFAC further clarifies that it looks to industry standards in determining whether goods or services were "fully provided or delivered" prior to the expiration of the applicable wind-down period. The FAQ guidance adds that, "[a]s a general matter, goods or services will be considered fully provided or delivered when the party providing or delivering the goods or services has performed all the actions and satisfied all the obligations necessary to be eligible for payment or other agreed-to compensation." For exports of goods to or from Iran, OFAC advises that title must at a minimum have been transferred for delivery to be considered complete.

U.S. Persons

By contrast, OFAC's updated FAQ guidance clarifies that wind-down general licenses authorizing certain Iran-related transactions by U.S. persons and non-U.S. entities owned or controlled by U.S. persons only permit the receipt of payments for qualified activities during the validity period of the authorizations. Thus, for example, because the wind-down general license authorizing certain transactions by non-U.S. entities owned or controlled by U.S. persons (at Section 560.537 of the Iranian Transactions and Sanctions Regulations, 31 C.F.R. Part 560) is only valid through 11:59 p.m. eastern standard time on November 4, 2018, payments may only be received for activities undertaken pursuant to the general license through that date and time.

A specific license from OFAC would be required for a U.S. person or non-U.S. entity owned or controlled by a U.S. person to receive any payments following the end of the relevant wind-down period. According to the updated guidance, a request for such licensing would be evaluated by OFAC on a case-by-case basis.

New Business Activities During Wind-Down Period

Finally, the updated FAQ guidance explains that OFAC generally would not consider the entry into a new contract or engaging in new business activity related to Iran during the relevant wind-down period to be sanctionable or prohibited new business in circumstances where the new contract or business (1) is in furtherance of a written contract or written agreement entered into prior to May 8, 2018, and (2) is necessary and ordinarily incident to the wind down of activities under the pre-May 8 contract or agreement. As an example, the relevant FAQ refers to "a new purchase order . . . entered into during the wind-down period if such business is contemplated under a Master Services Agreement entered into prior to May 8."

Updated EU Blocking Statute Enters Into Force

As outlined in our June 15 alert, the Blocking Statute has been amended to now apply to those extra-territorial sanctions on Iran that the United States is re-imposing.

The U.S. sanctions measures within the scope of the Blocking Statute are set forth in an Annex to the Blocking Statute (here) and are those addressed in our June 15 alert, specifically: certain restrictions under the Iran Sanctions Act of 1996, the Iran Freedom and Counter-Proliferation Act of 2012, the National Defense Authorization Act of Fiscal Year 2012, the Iran Threat Reduction and Syria Human Rights Act of 2012, and the Iranian Transactions and Sanctions Regulations.

Key Elements of the Blocking Statute

The European Commission has now issued guidance which to some extent addresses the main operative provisions of the Blocking Statute.

- Article 2: A person or entity to whom the Blocking Statute applies (referred to as an "EU operator") is obliged to inform the Commission that its economic and/or financial interests are directly or indirectly affected by the sanctions listed in the Annex within 30 days of receiving that information. The Guidance Note provides little detail on the process for making such a notification, beyond confirming the text of Article 2 which

states that all relevant information should be submitted either directly to the Commission or to the competent authority of a Member State.

- Article 5: This provision prohibits compliance with the requirements or prohibitions of the U.S. sanctions listed in the Annex. As discussed in our previous alert, Article 5 also makes provision for EU operators to request an authorization to comply with the extraterritorial legislation listed in the Annex if non-compliance would seriously damage their interests or those of the European Union. A template for such requests, which must be submitted to the European Commission, was published by the Commission on August 7 (here), together with an implementing regulation setting forth assessment criteria in evaluating Article 5 authorization requests (Commission Implementing Regulation (EU) 2018/1101 of 3 August 2018). Those criteria provide limited insight into the factors that the Commission will consider in deciding whether or not to grant such authorizations. The "non-cumulative" criteria include:
  - The existence of an ongoing administrative or judicial investigation against the applicant from, or a prior settlement agreement with, the third country which is at the origin of the listed extra-territorial legislation;
  - Whether measures could be reasonably taken by the applicant to avoid or mitigate the damage;
  - The adverse effect on the conduct of 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; and
  - Whether the applicant's activity would be rendered excessively difficult due to a loss of essential inputs or resources, which cannot be reasonably replaced.

  In the request for authorization, the applicant is expected to detail the provisions of the listed extra-territorial legislation with which it would need to comply and the precise activity in which it would otherwise seek to engage. The template expects applicants to demonstrate, including through supporting materials, why and how non-compliance would result in serious damage to the EU operator or the Union, and to set out the scope of the authorization being requested.
  The Commission has given no concrete indication of how swiftly applications will be considered, beyond advising that applications will be handled as soon as possible and that a final decision will be notified without delay. It is important to bear in mind that these applications will have no suspensive effect, meaning that while an application is pending, EU operators will still be under an ostensible obligation to comply with the Blocking Statute.

- Article 6: Under this provision, EU operators may recover damages in relation to losses suffered as a result of the application of the sanctions provisions listed in the Annex. An appropriate Member State court would hear such a claim and the defendant in such action would be the legal person or entity responsible for the damage. The Commission Guidance asks the question of whether Article 6 can be used by EU operators to seek redress directly from U.S. government authorities, but then does not directly answer that question, indicating instead that the question would need to be assessed by the competent court hearing the EU operator's claim. Any such claim by an EU operator against the U.S. government could potentially encounter sovereign immunity defenses, which the Commission Guidance does not address.

Practical Considerations

The Commission Guidance offers no assurance that license requests made under Article 5 will be granted, nor does it provide a roadmap for how the Blocking Statute should be enforced by the EU Member States against EU parties who determine to continue to "comply" with the U.S. sanctions listed in the Annex to the Blocking Statute. As the Blocking Statute has been effectively dormant since its initial passage in 1996, past precedent offers little insight in evaluating these issues.

In our view, EU parties should begin by assessing the following key threshold questions, the answers to which will depend on the specific nature of those parties' business activities in Iran and in Cuba (not losing sight of the fact that the Blocking Statute continues to apply, as it has since 1996, to certain aspects of the U.S.-Cuba sanctions):

- Is the reason why the EU party is not engaging in Iran- or Cuba-related transactions driven by U.S. trade controls restrictions, or by independent commercial or other legal considerations? For many EU companies, the limited nature of the Iran and Cuba markets, and quite independent legal concerns -- such as anti-money laundering, anti-bribery, financial regulatory, and litigation risk considerations -- may have caused those companies to limit or exclude Iran and Cuba from their business plans. For those companies, the implications of the Blocking Statute may prove to be inconsequential.
- If U.S. trade controls are motivating an EU party's decision not to pursue business with Iran or Cuba, the EU party must carefully consider whether that decision is being driven by the U.S. sanctions legal instruments listed in the Annex to the Blocking Statute, or by other aspects of the U.S. export controls and economic sanctions that are *not* covered under the Blocking Statute -- and, therefore, that EU parties are not prohibited from complying with.
- If EU parties determine to submit notifications or license requests under Articles 2 or 5, those parties may wish to consider whether to involve their local Member State authority in that process. For some EU companies, their Member State regulators may be in a better position than the Commission to ascertain and assess the legitimate interests of those companies in avoiding penalties under the U.S. primary sanctions or the imposition of U.S. secondary sanctions, and to balance those considerations against the aims of the Blocking Statute.

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Covington has deep experience advising clients on the legal, policy, and practical dimensions of U.S. and EU sanctions. We will continue to monitor developments in this area, including the planned re-imposition of additional U.S. sanctions on November 5 and the implementation of the EU Blocking Statute, and we are well-positioned to assist clients in understanding how these developments may affect their business operations.

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