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New Financial Sanctions Regulations Target Iranian Business Activities of Non-U.S. Financial Institutions

The U.S. Department of the Treasury, Office of Foreign Assets Control (OFAC), has issued new Iranian Financial Sanctions Regulations (IFSR) limiting access to the U.S. banking system of foreign financial institutions upon a finding by the United States that the financial institution (a) facilitates Iran's development of nuclear weapons or (b) provides financial services either to Iran's Islamic Revolutionary Guard Corp (IRGC) or to any financial institution whose property is blocked in connection with Iran's nuclear development or support of terrorism. The foreign financial institutions subject to these new prohibitions will be listed in an "Appendix A" to the new regulations, 31 C.F.R. Part 561. These regulations were issued under the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA). See, 75 Fed. Reg. 49,836.

Correspondent and Payable-Through Accounts. Under the IFSR, OFAC will terminate or severely restrict a foreign financial institution's access to the United States if they engage in any of the enumerated activities involving Iranian proliferation or terrorist activities. Specifically, the IFSR prohibit, or impose strict conditions on, the opening or maintaining in the United States of a "correspondent"¹ or "payable-through account"² for any foreign financial institution that OFAC finds knowingly:

1. Facilitates the efforts of the Government of Iran or the IRGC to acquire or develop weapons of mass destruction or provide support for terrorist organizations;
2. Facilitates the activities of a person subject to UN Security Council financial sanctions;
3. Engages in money laundering in support of the above activities;
4. Facilitates efforts by the Central Bank of Iran, or any other Iranian financial institution, to carry out the above activities; or
5. Facilitates a "significant transaction or transactions" or "provides significant financial services"³ for IRGC or its affiliates whose property is blocked pursuant to the International Emergency Economic Powers Act (50 U.S.C. 1701 et. seq.) ("IEEPA") or a financial institution identified on OFAC's SDN and Blocked Persons List by an "[IFSR]" tag in connection with Iran's proliferation or support for international terrorism.

If access is not prohibited outright, "strict conditions" imposed by the Treasury Secretary can include: a prohibition on the provision of "trade finance" through the account, restrictions on the types of and monetary limits for transactions, or a "pre-approval" requirement for all transactions processed through the account. 31 C.F.R. § 561.201(b)-(c).

Potential Parent Liability. The IFSR prohibit any person "owned or controlled" by a U.S. financial institution, from knowingly engaging in transactions with or benefiting the IRGC, its agents or affiliates, or Iranian financial institutions, whose property or interests in property are blocked by the United States and hence are Specially Designated Nationals. Although this prohibition relates to the activities of foreign subsidiaries or affiliates, the U.S. financial institution is potentially subject to civil or criminal penalties under IEEPA to the extent that the parent knew or should have known that its controlled subsidiary or affiliate attempted, conspired, or caused a violation of the regulations.

IEEPA currently provides for a maximum civil penalty not to exceed the greater of \$250,000 or an amount that is twice the amount of the transaction that is the basis of the violation. Criminal penalties involve a finding of "willfulness" and can include a fine of not more than \$1 million or 20 years imprisonment, or both.

Importantly, U.S. financial institutions should also expect OFAC to issue additional regulations implementing the audit and "due diligence" requirements of CISADA section 104(e). These will require U.S. financial institutions with foreign financial institution correspondent accounts to undertake one or more of the auditing and reporting activities described in section 104(e) to determine whether the foreign financial institution is engaging in any of the five activities set forth above.

CISADA's Impact. The adoption of these regulations is only one aspect of CISADA, which President

Obama signed into law on July 1, 2010. The Act, passed in the wake of comprehensive United National Security Council Resolution 1929 (2010), amends and substantially expands the coverage of the previous Iran Sanctions Act (ISA). Separate from the foreign financial institution provisions, the new law focuses on the activities of foreign persons and requires the President, who has been given circumscribed waiver authority, to impose sanctions on any person, either foreign or domestic, who engages in certain "sanctionable activities." Such activities relate to Iran's oil sector and encompass, subject to certain minimum monetary amounts, "knowingly" selling or providing refined petroleum products to Iran, and selling or providing goods, services, technology or support that would directly and significantly contribute to Iran's ability to import refined products or to the maintenance or expansion of Iran's domestic production of refined petroleum. These activities are in addition to knowingly making an investment of \$20,000,000 or more that directly and significantly contributes to Iran's ability to develop its petroleum resources.

Regarding these aspects of CISADA, at a July 29th Congressional hearing, a Senior Official from the U.S. State Department testified that CISADA "has yielded significant results" by contributing to decisions by "major international oil companies" and fuel suppliers not to undertake new business activities and investments in Iran related to its petroleum sector. In addition, as a result of the new law, international maritime insurer Lloyd's recently announced that it would stop underwriting gasoline imports to Iran; a move that analysts predict will prompt other major non-U.S. insurers to follow suit.

Many critical questions remain unanswered regarding the interpretation and implementation of CISADA. The Act places first line enforcement authority for this portion of CISADA in the U.S. Department of State, which has little experience at drafting or enforcing economic sanctions regulations. This raises the probability that regulations clarifying the meaning of vague yet critical terms in the statute will not be published quickly. Even so, CISADA's impact, insofar as its petroleum-related provisions are concerned, has already been significant.

Do you understand how CISADA may impact your international business activities? If not, please contact Venable's **International Trade and Customs Group** for assistance.

1. A "correspondent account" means an account established by a U.S. financial institution for a foreign financial institution to receive deposits from, or to make payment on behalf of, the foreign financial institution, or to handle other financial transactions related to such foreign financial institution.

2. A "payable-through account" means a correspondent account maintained by a U.S. financial institution for a foreign financial institution by means of which the foreign institution permits its customers to engage, either directly or through a subaccount, in banking activities usual in connection with the business of banking in the U.S.

3. In determining whether transaction(s) or financial services are "significant," OFAC may consider the totality of the facts and circumstances including, but not limited to: their size, number and frequency; their economic significance to the parties involved; their type, complexity or commercial purpose; the proximity or "nexus" between parties; whether "management" is involved or aware; whether there is a pattern of conduct; and/or whether deceptive financial practices were utilized.

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