

United States Re-Imposes Sanctions Against Iran: Impact on European Business

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International Trade Controls

On May 8, 2018, the United States [announced](#) the decision to end its participation in the Joint Comprehensive Plan of Action (“JCPOA”) and re-impose sanctions against Iran that had been suspended as part of this 2015 nuclear agreement between the United States, Iran, Germany, France, the UK and China.

U.S. relief from sanctions will be phased out over the next six months. This will have significant effects for European companies conducting business with Iran.

Following the U.S. announcement, the leaders of France, Germany, and the UK issued a [joint statement](#) emphasizing their “continuing commitment to the JCPOA.” There are no immediate reports that EU sanctions would be re-imposed, although the future course of EU sanctions may be determined, in large part, by whether European leaders are able to persuade Iran to continue implementing its commitments under the JCPOA (which involve limiting its nuclear capabilities and allowing international inspectors to verify). Furthermore, the EU governments are reportedly considering seeking exemptions to aspects of the re-imposed U.S. sanctions for European companies, although the likelihood of success of those efforts is uncertain.

In this alert, we briefly outline how the U.S. phase-out is expected to proceed, how the EU may react, and what actions companies can take to mitigate impacts.

Sanctions To Be Re-Imposed

The JCPOA took effect on January 16, 2016. Pursuant to the agreement, the United States and the EU extended broad sanctions relief to Iran in exchange for Iran accepting limitations on its nuclear program. Most “primary” U.S. sanctions remained in place under the JCPOA and, notably, continue to remain in place. The U.S. “primary” sanctions prohibit most direct or indirect business activities by U.S. persons with Iran, and also prohibit *non-U.S.* parties from involving U.S. persons in Iran-related business activities, or exporting or re-exporting certain types of restricted goods, software, and technology containing U.S.-origin content to Iran.

However, the JCPOA had significantly relaxed the U.S. “secondary sanctions” targeting non-U.S. persons that engage in certain types of business in Iran or with Iranian persons and entities. This relief will be phased out over the next six months. First, after a 90-day wind-down period ending on August 6, 2018, the U.S. government will fully re-impose an initial list of

sanctions. Second, after a 180-day wind-down period ending on November 4, 2018, the U.S. government will fully re-impose additional sanctions.

Sanctions Re-Imposed After 90 days

On **August 6, 2018**, the initial 90-day wind-down period will end. At that point, the U.S. government will re-impose the first group of sanctions targeting Iran that had been lifted under the JCPOA. Those sanctions include:

- Sanctions on the purchase or acquisition of U.S. dollar-denominated banknotes by the government of Iran;
- Sanctions on Iran's trade in gold or precious metals;
- Sanctions on the direct or indirect sale, supply, or transfer to or from Iran of graphite, raw or semi-finished metals such as aluminum and steel, coal, and software for integrating industrial processes;
- Sanctions on 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;
- Sanctions on the purchase, subscription to, or facilitation of the issuance of Iranian sovereign debt; and
- Sanctions on Iran's automotive sector.

Following the wind-down period that ends on August 6, 2018, the U.S. government will also revoke certain JCPOA-related authorizations that permitted:

- The importation into the United States of Iranian-origin carpets and foodstuffs and certain related financial transactions pursuant to general licenses;
- Activities pursuant to specific licenses related to the export and reexport of commercial passenger aircraft, issued under the JCPOA Statement of Licensing Policy for Activities Related to the Export or Re-export to Iran of Commercial Passenger Aircraft and Related Parts and Services ("SLP"); and
- Activities pursuant to General License I relating to contingent contracts for transactions that had previously been eligible for authorization under the JCPOA SLP. The U.S. Treasury Department's Office of Foreign Assets Control ("OFAC") will revoke General License I and publish a replacement authorization for wind-down activities.

OFAC advises persons engaged in any of the above activities to take the steps necessary to wind them down by August 6, 2018, in order to avoid sanctions and enforcement exposure.

Sanctions Re-Imposed After 180 days

On **November 4, 2018**, the 180-day wind-down period will end. At that point, the U.S. government will re-impose a second group of sanctions targeting Iran that had been lifted under the JCPOA. Those sanctions include:

- Sanctions on Iran's port operators, and shipping and shipbuilding sectors, including on the Islamic Republic of Iran Shipping Lines, South Shipping Line Iran, and their affiliates;
- Sanctions on petroleum-related transactions with, among others, the National Iranian Oil Company, Naftiran Intertrade Company, and National Iranian Tanker Company, including the purchase of petroleum, petroleum products, or petrochemical products from Iran;
- Sanctions on significant transactions by foreign financial institutions with the Central Bank of Iran and designated Iranian financial institutions under Section 1245 of the National Defense Authorization Act for Fiscal Year 2012;
- Sanctions on the provision of specialized financial messaging services to the Central Bank of Iran and Iranian financial institutions described in Section 104(c)(2)(E)(ii) of the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010;
- Sanctions on the provision of underwriting services, insurance, or reinsurance; and
- Sanctions on Iran's energy sector.

In addition to re-imposing the above-noted sanctions, beginning on November 5 the U.S. government will revoke authorization for U.S.-owned or -controlled entities outside the United States to wind down certain activities with the government of Iran or persons subject to its jurisdiction (which had previously been authorized under a general license, General License H, issued by the U.S. Treasury Department in connection with the entry into force of the JCPOA).

The U.S. government will also consider as subject to secondary sanctions activities with persons that have been reinstated to the U.S. List of Specially Designated Nationals and Blocked Persons ("SDN List"), and which under the JCPOA had appeared in a separate list known as the "E.O. 13599 List." That list includes persons that met the definition of the terms "Government of Iran" or "Iranian Financial Institution." Depending on the authority pursuant to which this re-listing occurs, secondary sanctions may attach to dealings with such persons following their re-designation on the SDN List.

As with the sanctions subject to a 90-day wind-down period, OFAC advises parties engaged in any of the above activities to wind them down within 180 days, or face exposure to U.S. sanctions or enforcement actions.

What Does OFAC Expect From Non-U.S. Companies During These "Wind-Down" Periods?

In general, European entities that are not owned or controlled by U.S. persons (for purposes of the U.S. primary sanctions) are expected by the United States (i) not to engage in new activity involving Iran that could trigger secondary sanctions; and (ii) to wind down existing activities in Iran that could trigger secondary sanctions. Such European entities also must ensure that they fully comply with the U.S. primary sanctions in connection with any ongoing or future business activities relating to Iran, including by ensuring that U.S. persons are not directly or indirectly involved in Iran-related business, and that no goods, software, or technology containing restricted U.S. content are re-exported to Iran in circumstances that would violate the primary sanctions. In addition, European companies that are owned or controlled by U.S. persons will also need to begin winding down activities that previously had been authorized under General License H.

The wind-down process for European and other non-U.S. companies is subject to the following specific allowances:

- In situations where non-U.S., non-Iranian persons (i) had a written contract or written agreement in effect prior to May 8, 2018, to provide goods or services to an Iranian counterparty that was consistent with then-governing sanctions; and (ii) have fully completed the provision or delivery of such goods or services to the Iranian counterparty prior to the end of the applicable wind-down period, the non-U.S., non-Iranian person may collect any payments owed for such goods or services *after the applicable wind-down period expires* without being exposed to U.S., secondary sanctions, if the collection is pursuant to the terms of the written contract or agreement.
- In situations where non-U.S., non-Iranian persons (i) had a written contract or written agreement in effect prior to May 8, 2018, to extend a loan or credit to an Iranian counterparty that was consistent with then-governing sanctions; and (ii) extended such loan or credit prior to the end of the applicable wind-down period, the non-U.S., non-Iranian person may receive repayment of the debt or obligation according to the terms of the written contract or agreement *after the applicable wind-down period expires* without being exposed to U.S. secondary sanctions.

OFAC has explained that these allowances are “designed for non-U.S., non-Iranian parties to be made whole for debts and obligations owed or due to them for goods or services fully provided or delivered or loans or credit extended to an Iranian party prior to the end of the 90-day or 180-day wind-down period, as applicable.” OFAC has cautioned that any payments made pursuant to this wind-down “allowance” may not involve U.S. persons or the U.S. financial system unless authorized by OFAC or otherwise exempt.

The potential application of the U.S. sanctions to European companies was reinforced last week by U.S. ambassadors from Germany and several other European countries, who publicly warned European companies, in general terms, against continuing to trade with Iran. If European companies were to engage in conduct triggering U.S. secondary sanctions, those actions could result in the imposition of retaliatory trade actions against the European company by the United States government, including measures that could effectively serve to prohibit the European company from doing business in the United States or with U.S. persons. Violations of the primary U.S. sanctions could expose a European company to substantial civil or (in the case of willful violations) criminal penalties.

Response From The European Union

As noted, reports over the last several days indicate that EU governments are considering petitioning the U.S. government for exemptions that would allow European companies to continue engaging in business activities with Iran that might otherwise trigger secondary sanctions. It is, however, uncertain whether those measures will receive a positive reception in Washington.

If the EU and United States are not able to reach such an accommodation, the EU could consider taking more assertive action. Such action could include, for instance, challenging the application of the U.S. secondary sanctions before the World Trade Organization (“WTO”), on the basis that these secondary sanctions represent an impermissible restraint on international trade. The European authorities had, notably, threatened WTO action when the first U.S.

secondary sanctions regime was implemented in 1996 (the U.S. Iran and Libya Sanctions Act of 1996). That step, along with agreement by the EU to cooperate with the United States on antiterrorism and anti-proliferation matters, resulted in a waiver by the U.S. government of secondary sanctions for a specific project being undertaken at that time by a European company and its partners, together with a tacit policy by the United States of not actively enforcing the secondary sanctions. It is, however, unclear whether the U.S. government would be amenable to such a resolution in the current political climate and what additional assurance the EU would be prepared to offer.

The EU also could respond by re-invigorating its blocking regulation (EC Regulation No. 2271/96). That regulation, which was implemented in 1996 and remains in force, prohibits EU parties from complying with certain U.S. sanctions programs, including aspects of the U.S.-Cuba sanctions and aspects of the U.S.-Iran secondary sanctions that were implemented in 1996. If it were to be utilized to combat the U.S. departure from the JCPOA, the blocking regulation would need to be amended to reflect the current U.S. secondary sanctions (most aspects of which were implemented after 1996), and it would need to be enforced. Indeed, the blocking regulation has been subject to only sporadic enforcement in the 22 years it has been in place. If that were to occur, it could place EU companies in a very significant conflict of law position.

In addition, German companies could face national law risks due to the anti-boycott provision in the German Foreign Trade Act (AWG/AWV), which prohibits any agreement to comply with sanctions against another state that go beyond the German or EU regulations. Any intentional or negligent non-compliance with the German regulation constitutes an administrative offence which can be sanctioned by a fine up to EUR 500,000.

Efforts by European companies to terminate contracts in light of the U.S. secondary sanctions would also potentially run the risk of commercial liabilities, particularly if the contracts in question did not contain clear clauses allowing for termination in the event pre-JCPOA sanctions were reintroduced.

Finally, the EU response to the U.S. decision to end its participation in the JCPOA will also be substantially informed by events in Iran. If Iran were to react to the U.S. actions by terminating its efforts to reduce its nuclear capabilities, it is conceivable that the entire JCPOA could collapse and the EU could reintroduce aspects of the EU sanctions regime that were in place prior to the JCPOA. However, reports over the last week make clear that the intent of the EU authorities is to work to secure continued cooperation from Iran, in return for continued access to EU markets and suppliers.

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Covington has deep experience advising clients on the legal, policy, and practical dimensions of U.S. trade controls, including Iran sanctions. We will continue to monitor developments in this area, including responses by the EU to the United States' withdrawal from the JCPOA. We are well-positioned to assist clients in understanding how these recent actions may affect their business operations.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our International Trade Controls practice:

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