KIRKLAND & ELLIS

KIRKLAND **ALERT**

October 2012

U.S. Presidential Order Marks Start of U.S. Sanctions Liability for Foreign Subsidiary Business With Iran, OFAC Provides Limited Guidance

On October 9, 2012, the U.S. president signed an Executive Order, "Authorizing the Implementation of Certain Sanctions Set Forth in the Iran Threat Reduction and Syria Human Rights Act of 2012 and Additional Sanctions with Respect to Iran," (the "Order"). The Order implements certain statutory requirements of the Iran Threat Reduction and Syria Human Rights Act of 2012 ("TRA"), including Section 218, making foreign subsidiaries or foreign entities "owned or controlled by" U.S. companies subject to prohibitions on trade with Iran covered by the International Emergency Economic Powers Act ("IEEPA"). On the same day, the U.S. Department of the Treasury, Office of Foreign Assets Control ("OFAC") issued guidance on the TRA, including Section 218 (Frequently Asked Questions Related to Section 4 of the Executive Order). TRA was signed on August 10, 2012. See Kirkland & Ellis' September 2012 Alert regarding Iran Sanctions. The Order and OFAC announcement likely will disappoint many companies hoping for additional concrete guidance on how to best proceed in compliance with the TRA.

As of October 9, 2012, pursuant to the Order, a U.S. company is liable for any activity "knowingly" engaged in with Iran, directly or indirectly, by a foreign affiliate that it owns or controls ("foreign subsidiary"), in which a U.S. person is prohibited from engaging under existing U.S. sanctions. The Order defines "knowingly" to include actual knowledge, as well as a situation in which an entity "should have known of the conduct, the circumstance, or the result." Any violation of or attempt to violate by a foreign subsidiary this effective prohibition on foreign subsidiary activity will subject the U.S. company to potential civil penalties for each violation of up to $250,000, or twice the value of the transaction. A single transaction may involve multiple violations.

Neither the Order nor OFAC guidance provides any additional avenues for "winding down" foreign subsidiaries' existing contracts, which many in the international business community had hoped may be forthcoming. Divestiture or termination of business with foreign subsidiaries that have business with Iran that is now prohibited under TRA and the new Order is the only "wind down" or "safe harbor" cited in OFAC's guidance.

U.S. enforcement authorities from OFAC and the U.S. State Department have indicated that they are willing to engage companies to discuss specific cases of "winding down" contracts beyond the 180-day termination period, which may involve compelling "national security" or "national interest" implications. OFAC has indicated the standard would be the same as applied currently for granting specific licenses to U.S. parties, which is relatively limited. In the case of exports to Iran, OFAC also has indicated that the exporter will be responsible for proving that the good is not "controlled" using the U.S. export control law standards.

Foreign subsidiaries engaged in export of agricultural, pharmaceutical and medical device goods to Iran, may apply, as U.S. companies now do, for a specific OFAC license pursuant to the Trade Sanctions Reform and Export Enhancement Act of 2000 ("TSRA"). Non-governmental organization foreign subsidiaries also may be granted licenses for their humanitarian work in Iran. OFAC's guidance further confirms that all exemptions and general authorizations under existing Iran sanctions also would apply to foreign subsidiary activity. For instance,

Attorney Advertising

exemptions and general authorizations exist as to travel, providing information or informational materials, intellectual property protection and certain humanitarian activities related to Iran.

The Order and OFAC guidance do not provide any further clarification of the definition of "control." TRA defines ownership and control of a foreign subsidiary as any of the following:

- More than 50 percent of the equity interest by vote or value;
- A majority of the seats of the board of directors; or
- Control otherwise of the actions, policies, or personnel decisions.

The Order implements many other TRA provisions, pertaining for instance to the Iran Sanctions Act ("ISA") and Comprehensive Iran Sanctions and Divestment Act ("CISADA") targeting petroleum related transactions, and financial institution transactions related to Iran. As with Section 218 of TRA, the Order largely tracks the existing TRA language. In a letter from the president to Congress, the president explains that the Order also intends to ensure that ISA sanctions authority is in effect for activity occurring in the period between the effective dates of CISADA and TRA, *i.e.*, July 1, 2010, and August 10, 2012.

The primary take-away for many international businesses from the October 9 actions is that the February 6, 2013, "safe harbor" for U.S. companies to divest or terminate foreign subsidiary business means difficult decisions and actions are ahead. While engaging U.S. enforcement authorities always presents potential downside issues, companies should evaluate whether a compelling "national interest" case may be made to U.S. authorities that may warrant specific authorization or guidance.

If you have any questions about the matters addressed in this *Kirkland Alert*,
please contact the following Kirkland authors or your regular Kirkland contact.

Laura Fraedrich
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/lfraedrich
+1 (202) 879-5990

Michael J. Garcia
601 Lexington Avenue
New York, NY 10022
www.kirkland.com/mgarcia
+1 (212) 446-4810

Joanna M. Ritcey-Donohue
655 Fifteenth Street, N.W.
Washington, D.C. 20005
www.kirkland.com/jritcey-donohue
+1 (202) 879-5980

This communication is distributed with the understanding that the author, publisher and distributor of this communication are not rendering legal, accounting, or other professional advice or opinions on specific facts or matters and, accordingly, assume no liability whatsoever in connection with its use. Pursuant to applicable rules of professional conduct, this communication may constitute Attorney Advertising.

© 2012 Kirkland & Ellis LLP. All rights reserved.

www.kirkland.com