

INTERNATIONAL TRADE

INTERNATIONAL SANCTIONS AGAINST IRAN, LIBYA AND SYRIA JUNE 2011

Introduction

This is the latest in our series of updates on international sanctions and should be read in conjunction with the previous updates, which are available on the Ince & Co LLP website at www.incelaw.com.

The last 12-18 months have been a busy period for the imposition of international sanctions against various countries and entities across the globe. Events in the Middle East and North Africa have precipitated an increase in the use of economic sanctions as a tool to try to put further pressure on various regimes to alter their policies and to “encourage” them to refrain from actions disapproved of by the international community. The wide-ranging reach of sanctions legislation introduced primarily by the UN, US and EU, and the consistent interest of the media in reporting possible sanctions breaches has made sanctions a prominent focus area for the shipping industry and international traders. The high profile of sanctions in the news and the risk of adverse media coverage in the event of breach, not to mention the penalties and fines that may result from their breach, means it remains of vital importance that international businesses carefully consider their operations within the framework of sanctions legislation and ensure that they have effective compliance programs in place.

This article provides an overview of the recent events relating to sanctions against Iran, Libya and Syria.

Iran

It is just over a year since UN Security Council Resolution 1929 was passed, imposing additional sanctions on Iran. The Resolution formed the basis for a raft of sanctions subsequently introduced by various countries around the world, but in particular for new legislation from both the US and EU authorities. On 1 July 2010, the Comprehensive Iran Sanctions, Accountability and Divestment Act 2010 (“CISADA”) entered into force in the US amending the existing Iran Sanctions Act 1996. This was followed on 27 October 2010 by the implementation of EU Regulation 961/2010 concerning restrictive measures on Iran. The main aim of these sanctions has been to stop Iran’s nuclear programme by implementing measures imposed on the energy industry in Iran and making any trade with the country practically and commercially difficult.

We comment below on recent EU and US developments.

Recent developments - EU Legislation

On 24 May 2011, EU Regulation 503/2011 entered into force. This amended EU Regulation 961/2010 adding a large number of entities to the list of EU sanctioned persons, including a number of companies based in Germany and the Isle of Man. Many of the entities listed in the new Regulation are said to be linked to IRISL who have been targeted heavily by global sanctions.

Other companies designated as sanctioned persons in the new Regulation include many other front companies and entities used by sanctioned entities and individuals. It appears that a number of sanctioned entities have sought to use front companies located in offshore jurisdictions such as Malta and the Isle of Man to try and circumvent the operation of the restrictions. The geographical location of these front companies is of note as they are jurisdictions where many legitimate non-sanctioned ship owning companies and charterers are based.

International authorities are continually investigating the links between sanctioned entities and other parties and it is therefore extremely important that full and proper due diligence is carried out on any counterparty and transaction that may have a link to Iran and/or to Iranian entities. One of the key matters to keep in mind when carrying out such due diligence is whether any of the parties involved in the transaction may be ultimately owned or controlled by a sanctioned entity. If, following the due diligence inquiries, any suspicions are raised about a transaction and, assuming that they cannot be resolved satisfactorily through the exercise of further due diligence, then it is better to adopt a risk averse approach and pull out rather than risk breaching the sanctions with the penalties that that brings with it.

Recent developments – US Legislation*

There have been a number of significant developments relating to Iranian sanctions in the US in the past few weeks. These have included enforcement action being taken against non-US based entities for breaches of sanctions as well as the designation of Iran Air and Tidewater Middle East Company as sanctioned entities. We comment on these developments and their significance overleaf.

US imposes sanctions on Tidewater Middle East Company and Iran Air

On 23 June the US Treasury designated two major Iranian commercial entities Tidewater Middle East Co. and Iran Air as sanctioned entities. (Tidewater Middle East Co. should not be confused with Tidewater Inc., a leading provider of marine support services for the offshore energy industry based in the US. The US Department of the Treasury Fact Sheet makes clear that Tidewater Middle East Co. is separate and distinct from Tidewater Inc., and that sanctions have not been imposed on Tidewater Inc.)

Tidewater Middle East Co. is a port operating company owned by Iran's Revolutionary Guard Corps ("IRGC") and is said to have been used by the IRGC for illicit shipments. Tidewater Middle East Co. has operations at seven Iranian ports as set out below:

- > Bandar Abbas (Shahid Rajaei Container Terminal)
- > Bandar Imam Khomeini Grain Terminal
- > Bandar Anzali
- > Khorramshahr Port
- > Assaluyeh Port
- > Aprin Port
- > Amir Abad Port Complex.

The Fact Sheet published by the US Department of the Treasury states that Tidewater Middle East Co. managed ports in Iran have repeatedly been used by the Iranian Government to export arms or related material in violation of United Nations Security Council resolutions. The designation of Tidewater Middle East Co. by the US means that no US company will be able to do business with Tidewater Middle East Co. Further, any assets held by Tidewater Middle East Co. in the US will be frozen.

While Tidewater Middle East Co. has, so far, only been designated by the US, it is possible that the EU will follow suit in short order. In any event, however, in light of recent enforcement action taken by the US (see below) this designation is likely to create significant difficulties for those trading with Iran as Tidewater Middle East Co. provides extensive services at the ports listed above including container loading and unloading; customs release services; shipping services; unloading and loading of bulk goods and marine services. Any company trading to Iran will now need to carefully check whether the above ports are involved as shipping firms that knowingly do business with Tidewater Middle East Co. could be barred from dealing with U.S. financial institutions. These designation by the US authorities could effectively prevent vessels from calling at these ports as many of the services for vessels may be solely provided by Tidewater Middle East Co. As always it is also important to ensure that payments are not made to third parties acting on behalf of a sanctioned person in order to circumvent the operation of the sanctions

Iran Air, Iran's national air carrier has also been designated for providing support and services to Iran's Ministry of Defence and Armed Forces Logistics and the IRGC through the transport and/or transfer of goods, for or on behalf of, these entities. Rockets or missiles have been transported via Iran Air passenger aircraft and commercial Iran Air flights are also said to have been used to transport missile or rocket components to Syria.

As with Tidewater Middle East Co., the designation of Iran Air by the US means that no US company will be able to do business with it and any assets held by Iran Air in the US will be frozen.

US enforcement action against non-US entities

When CISADA was introduced by the US authorities it gave rise to concern within the international community as it was clear from the way it was drafted that it was intended to have extra-territorial effect. In other words, it applies to all persons, wherever located, and is not restricted to US persons or those based within the US jurisdiction.

Under the legislation, where a party is found guilty of breaching sanctions, the President is required to impose at least three penalties of those which are available to him. Although the penalties are effective within the US jurisdiction they can still have a significant impact on companies operating or based outside the US. For example, penalties which could be imposed include a restriction on payments being made through the US banking system and a freeze of assets located within the US.

Until recently, the US had not taken significant enforcement action against companies based outside US jurisdiction who were in breach of US sanctions legislation. However, on 24 May 2011, the US State Department issued a fact sheet detailing the sanctions that had been imposed on seven companies found guilty of breaching sanctions. We comment on these developments below:

Sanctions imposed on PCCI and other refined petroleum suppliers

Sanctions have been imposed on PCCI (Jersey) and two UAE companies for supplying refined petroleum products to Iran. They are said by the US State Department to have "regularly engaged in deceptive practices in order to ship these products to Iran and evade US sanctions".

As a result of the sanctions imposed against these companies they are restricted from US foreign exchange transactions; US banking transactions and all US property transactions. The severity of the penalties reflects that the companies were actively engaging in deceptive practices intended to evade US sanctions.

PDVSA

The US has sanctioned the Venezuelan State owned oil company, Petroleos De Venezuela SA ("PDVSA") for providing cargoes of reformate to Iran between December 2010 and March 2011 worth in the region of US\$ 50 million. Reformate can be used to assist in the refining of gasoline - a key target of the US sanctions.

The three sanctions imposed against PDVSA prohibit the company from competing for US Government procurement contracts; securing financing from the Export-Import bank of the US; and obtaining export licences.

It is, however, worth noting the following key points about the sanctions that have been imposed against PDVSA:

- > PDVSA is not listed as a sanctioned entity on the US 'Specially Designated Nationals' list - it is not "black-listed".
- > The sanctions do not apply to PDVSA subsidiaries - importantly PDVSA own the US Company CITGO which

operates a number of refineries and petrol stations in the US, employing US workers. If PDVSA subsidiaries had been impacted by the sanctions, it is likely that this may have had an impact on Citgo's operations and therefore affected the US economy directly.

- > The sanctions do not prohibit the export of crude oil to the US.

Sanctions imposed for lack of due diligence

In addition to the above, the US State Department also sanctioned two other companies for their alleged role in the sale of a tanker to IRISL, the sanctioned Iranian shipping line.

This development underscores the importance of carrying out thorough compliance and due diligence checks as in a statement released by the US State Department it was said that the companies "had failed to exercise due diligence". Under the US legislation companies can be held accountable when they either know or "should have known" that they were providing sanctionable goods or services to Iran. The US authorities have taken this approach in this case on the basis that they considered that the companies could have discovered that the vessel was going to IRISL through proper checks on the information that was publicly available. The restrictions placed on these companies prevent them from obtaining financing from the Export-Import bank of the US; obtaining loans over \$10 million from US financial institutions; and receiving US export licences.

In addition, the brokers involved in the transaction were sanctioned for their role. They are said to have knowingly acted on behalf of an IRISL front company and they are accordingly restricted from US foreign exchange transactions; US banking transactions and all US property transactions. These penalties are more severe than those placed on the other companies and demonstrate the enforcement of sanctions where someone is found to have knowingly breached the US restrictions.

It has been reported that some of the above entities are in discussions with the US authorities with a view to the sanctions, which they say have been wrongly imposed upon them, being lifted.

In relation to the sanctions imposed on the companies involved in the sale of the IRISL vessel (except for the brokers) it is worth noting that they are not the most severe sanctions that could have been imposed by the US authorities. Although the entities were not listed as sanctioned persons, the ability of the US to impose stricter penalties on those who breach sanctions means that it is important that this legislation is considered carefully and not just by those with a clear US involvement.

The enforcement action taken by the US against these non-US companies reflects the extra-territorial effect of the US legislation and the need for all businesses to carry out full and extensive due diligence to ensure compliance with sanctions legislation. Where any doubt exists about any transaction a risk averse approach should be taken. Further information should be sought and where questions or suspicions still remain the transaction should not proceed.

Now that the considerable resources of the US State Department are being employed in addition to those of the US Treasury to investigate sanctions breaches, it seems likely that more enforcement action will follow in the future.

Indictment of IRISL

In addition, on 20 June 2011, the New York District Attorney's Office issued an indictment against companies connected to IRISL for their alleged illegal use of banks in Manhattan. The indictment follows investigations into IRISL's alleged use of *'aliases or corporate alter egos'* to hide the processing of millions of dollars of payments through the New York banks. The indictment charges those involved with a conspiracy to conduct business in US dollars after the sanctions introduced against IRISL and sanctioned affiliates prohibited them transacting with or through US financial institutions. By using substitute names, the payments were processed through the financial institutions when they would otherwise have been blocked. On the same day, the US Treasury Department designated as sanctioned persons a further ten companies and three individuals said to be linked to IRISL. It remains to be seen what effect this indictment will have where those involved are located outside US jurisdiction but it does demonstrate the US's concerted effort to investigate and pursue sanctions breaches.

Libya

Further to our last update on Libya, NATO forces continue to oversee military action in Libya in support of UN Resolution 1973. With the conflict between forces loyal to the Qadhafi regime and the rebel forces continuing, the sanctions against those individuals and entities supportive of the Qadhafi regime are increasing. The authorities are seeking to pressurise the Qadhafi regime by restricting funds and economic resources; by targeting Qadhafi controlled companies and preventing the shipment of key resources to the regime. The rebels have set up the National Transitional Council as a representative body conducting the diplomatic relations of the rebels. Many international countries have recognised this body as the legitimate representative of the Libyan people including the UK, Spain, Germany, France, Italy, the UAE, Qatar and Australia. It is important to note that, as with EU sanctions legislation on Iran, funds and economic resources must not be made available directly or **indirectly** to sanctioned persons.

The latest sanctions are designed to prevent key resources from being acquired by the Qadhafi regime.

Designation of Libyan ports

On 17 June 2011, EU Regulation 572/2011 was implemented. This imposed an asset freeze on various ports in Libya. The ports have been listed for an asset freeze because they are identified as belonging to the Qadhafi regime. The list of sanctioned ports is as follows:

- > Port Authority of Tripoli
- > Port Authority of Al Khoms
- > Port Authority of Brega
- > Port Authority of Ras Lanuf
- > Port Authority of Zawia
- > Port Authority of Zuwara.

The impact of an asset freeze will affect the shipping industry. Those who are also involved in Ivory Coast trade will recall a similar freeze of the main ports of the Ivory Coast earlier this year following the disputed Presidential election. In effect, the sanctions against Port authorities prohibit all vessels from trading with those destinations. The restrictions will prevent the payment of fees to port authorities and other dues and expenses which allow a vessel to berth at the port.

Exemptions can be authorised for payments made until 15 July 2011 for contracts entered into prior to 7 June 2011. However, as per HM Treasury guidance, licences and exemptions will not be granted where those contracts are related to oil, gas and refined products – key resources required by the Qadhafi regime and military. By restricting the trade in these key materials to the Western part of Libya controlled by Qadhafi, it is hoped that the regime will face further pressure. As the situation in Libya escalates and the authorities investigate supply lines to Qadhafi, it is likely that further individuals and entities will become subject to restrictions. With an ever changing conflict, it is important that companies trading with Libya and neighbouring countries are aware of the restrictions in place.

Syria

In recent weeks, there has been increasing media coverage of the unrest that is unfolding in Syria including the recent internal military action. EU authorities are seeking to increase pressure on the regime and it is likely that more sanctions will be introduced in addition those currently in force. On 10 May 2011, EU Regulation 442/2011 was implemented which introduced restrictive measures on Syria. This follows the format of other EU sanctions legislation and imposes asset freezes on designated persons, entities and bodies and restrictions on the provision of economic resources to them. The most notable individual identified to date is Bashar Al-Assad the President of Syria. On 24 June 2011, EU Regulation 611/2011 was implemented adding a further seven individuals and four entities to the list of those against whom sanctions have been imposed.

It is therefore important to check that those companies that you may be transacting business with that are linked to Syria are not owned or controlled either directly or indirectly by one of the listed sanctioned persons.

What risk factors should you be looking for in transactions?

There are certain 'red flags' which, if raised in relation to a transaction, indicate that further due diligence or investigation may be required. By way of summary, some of the common issues which may indicate the need to carry out further due diligence are as follows:

Lack of information – for example the failure of a counterparty to provide information about the shareholders or beneficial owner of a company even on a confidential basis.

Diversions risk countries – certain countries are known to be a transshipment destination prior to cargo being delivered to a sanctioned country such as Iran. Questions which should be considered include - "Are the goods of the usual type to go to that country?". If not then further investigation may be needed especially where goods are being delivered in close proximity to a country subject to wide international sanctions.

Contractual Documents – are Bills of Lading or transactional documents unmarked or to the order of the counterparty? It is important to check contractual documents to ensure that they do not list sanctioned persons e.g. a sanctioned bank noted on the Bill of Lading.

Will "Sanctions Clauses" assist?

Sanctions clauses can be drafted to try to protect your position under a contract. Although BIMCO and INTERTANKO have produced standard sanctions clauses for charterparties, it is important that any clause is tailored to your specific needs under a contract. The inclusion of warranties and a mechanism to deal with sanctions issues can assist the parties in formulating their respective rights should the legislation change or further information become available. Where sanctions clauses are being incorporated into contracts it is important that care is taken to ensure the clause covers the eventualities you are seeking to protect yourself from.

Summary

With economic sanctions becoming an ever more important tool in the armoury of governments to combat terrorists, violent regimes and military procurement, it is important to keep up to date and consider how sanctions can affect your business. It is likely that sanctions legislation will continue to develop and as such the due diligence that is required is also likely to increase. Internal compliance programs should therefore be continually reviewed and updated to take into account developments.

The above summarises some recent developments but is not intended to act as an alternative to obtaining legal advice. If sanctions issues arise in your business we recommend that you contact your usual contact at Ince & Co LLP or speak direct to Michelle Linderman.

* Note: We are not qualified to advise on US law, however, we can provide recommendations if you require assistance from US lawyers.



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