GIBSON DUNN

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IRAN STEPS BACK FROM NUCLEAR DEAL AS TRUMP ADMINISTRATION INCREASES SANCTIONS PRESSURE

To Our Clients and Friends:

May 8, 2019, was the one-year anniversary of the U.S. decision to withdraw from the 2015 Iran nuclear deal, formally known as the Joint Comprehensive Plan of Action ("JCPOA"), and it was eventful. The day began with Iranian President Hassan Rouhani announcing that Iran would immediately suspend compliance with JCPOA limits on enriched uranium and heavy water, with further suspensions to occur in 60 days unless assurances are made that Iran will receive promised economic benefits in the oil and banking sectors. Later that day, the Trump administration imposed new sanctions relating to the iron, steel, aluminum, and copper sectors of the Iranian economy. These new sanctions are the latest in what the White House is calling the "most powerful maximum pressure campaign ever witnessed."[1]

The pressure campaign has indeed ramped up in the past month. First, on April 8, the U.S. State Department designated the Islamic Revolutionary Guard Corps as a foreign terrorist organization—marking the first time an arm of a foreign government has received such a designation. Next, on April 22, the Trump administration declined to renew sanctions waivers that allowed certain countries to import Iranian oil. Then, on May 3, the administration declined to renew two sanctions waivers—one allowing Iran to store excess heavy water produced in the uranium enrichment process, and another allowing Iran to trade away its enriched uranium.

The ramifications of these recent events are global in scale. Iran will likely see its recession deepen, as new U.S. restrictions threaten two pillars of its export economy: crude oil and industrial metals. Given that Iran has been increasingly pushed into a corner, it is no surprise that the country has threatened to violate its JCPOA commitments in hopes of relief. So far, the signatories still in the deal—China, France, Germany, Russia, and the United Kingdom—have not taken concrete action in response, but that may change if Iran follows through with its threats. In the meantime, Iran's main customers, which include China and India, will need to find alternative trade partners or else face consequences under U.S. sanctions laws. These recent developments also complicate bilateral trade talks between the United States and China, which have stalled this week. Finally, given that the Trump administration has not shied away from using economic sanctions as a political tool, we could see waivers of sanctions liability under Iran sanctions used as a bargaining chip.

We discuss below these recent developments, in the order in which they occurred. To understand the lead-up to these events, please see the many client alerts we have published on the constantly evolving state of Iran sanctions—the most recent being our 2018 Year-End Sanctions Update.

Designation of the IRGC as an FTO

On April 8, the Treasury Department designated the Islamic Revolutionary Guard Corps ("IRGC"), an official part of Iran's government, as a foreign terrorist organization ("FTO").[2] The IRGC has already been designated and blocked under various sanctions programs—including those relating to counterterrorism. What is surprising here is that the FTO label has, until now, been exclusively used on non-state actors such as Al-Qaeda or the Islamic State of Iraq and Syria ("ISIS").

While the new legal ramifications are two-fold, we do not expect these changes to have a significant impact on U.S. and non-U.S. person decisionmaking as to whether to engage the IRGC and its many associated entities in business transactions. First, due to the FTO designation, IRGC members can be excluded from entering the United States by virtue of their affiliation.[3] Second, any person who knowingly provides material support or resources to the IRGC can be criminally prosecuted or subject to civil enforcement for doing so under separate FTO authorities.[4] Prior to this new designation however and subject to both criminal and civil enforcement, no U.S. person or non-U.S. person whose transactions had a nexus to the United States could do business with the IRGC without OFAC authorization. Moreover, non-U.S. persons were also already potential targets for designation themselves or of secondary sanctions for doing business with the IRGC and its associated entities. Given these already existing sanctions, it is unclear whether the largely duplicative enforcement powers the administration has gained through the designation outweigh the concern expressed by some that the IRGC's FTO designation will increase the risk to U.S. servicepersons by, among other things, shutting down communication channels that might be helpful in the United States' fight against ISIS.[5] It remains to be seen whether the EU decides to expand the reach of the EU Blocking Statute to counter the FTO designation.

Non-Renewal of Iran Oil Waivers

As part of its withdrawal from the JCPOA, the Trump administration re-imposed the possibility of secondary sanctions on importers of Iranian oil last November. To cushion the blow, temporary waivers[6] of those sanctions were granted to eight jurisdictions: China, India, South Korea, Japan, Italy, Greece, Taiwan, and Turkey.[7] Our contemporary analyses of the temporary waivers, also known as Significant Reduction Exceptions ("SREs"), can be found here and here. Those waivers expired on May 2, 2019.

Ahead of the expiration date, on April 22, 2019, Secretary of State Michael Pompeo announced that no further SREs would be issued,[8] a surprising move in light of reports that some State officials had promised additional waivers.[9] In his statement, Pompeo assured the public that global oil markets would continue to be well supplied in the absence of waivers, citing productive discussions with Saudi Arabia, the United Arab Emirates, and other major oil producers.[10]

The expiration of the SREs has little effect on Taiwan, Italy, and Greece, which reportedly ceased importing oil from Iran long before Pompeo's announcement.[11] The other SRE recipients, on the other hand, continued to purchase Iranian oil in early 2019; in fact, China increased its purchases, cementing its status as Iran's biggest customer.[12] China's foreign ministry representative spoke out against the non-renewal decision, expressing opposition to the Trump administration's "unilateral sanctions" and urging it to avoid "wrong moves" relating to Iran oil controls.[13] Turkey's foreign minister made a similar statement, also characterizing the Iran oil sanctions as "unilateral."[14]

At this early stage, it is unclear what practical effects the expiration of the SREs will have. For example, can the countries with expired SREs continue to take delivery of already-purchased Iranian oil, or use money already set aside to make additional purchases? These questions were apparently posed to two senior Department of State officials, but the officials characterized them as "hypothetical" and thus refused to comment.[15] Another question is whether drawing on Iranian oil from storage will trigger sanctions. Indeed, China reportedly has 20 million barrels of oil (worth over $1 billion) currently in storage in the northeast port of Dalian.[16]

As we have previously outlined, there are still narrow categories of authorized activities, such as those supported by: (1) General License J-1, allowing non-U.S. persons to fly U.S.-origin civil aircraft into Iran; (2) General License D-1, authorizing U.S. persons to export certain hardware, software, and services incident to personal communications over the Internet; and (3) various humanitarian exceptions allowing the export of agricultural commodities, food, medicine, and medical devices to Iran. The current SREs support and promote transactions in the third category because, under this regime, payments to Iran for its oil are held in escrow accounts that Iran can *only* use for the purchase of humanitarian (or otherwise non-sanctioned) goods.[17] If the expiration of the SREs has the intended effect of depriving Iran of oil revenue, then the country may not have the funds to purchase non-sanctioned goods to the same extent that it has in the past.

Non-Renewal of Two Waivers and Shortened Renewals of Five Waivers for Civilian Nuclear Activities

On May 3, the State Department announced that five sanctions waivers relating to civilian nuclear projects in Iran would be renewed, but for 90 days rather than the usual 180 days and with an added caveat that any effort starting May 4 to expand the Bushehr nuclear power plant would be subject to sanctions.[18] Two waivers, however, were not be renewed. The first waiver allowed Iran to store excess heavy water outside of the country; its expiration will pressure Oman, where Iran's heavy water is currently stored, to dispose of it. The second waiver allowed Iran to trade its enriched uranium for natural uranium, which is explicitly authorized by the JCPOA; the end of this waiver will most impact Russia, who has been a key player in these trades.

This mixture of renewals and non-renewals reflects the Trump administration's attempt to apply pressure on Iran without upending the nuclear status quo. U.S. National Security Adviser John Bolton has reportedly pushed to end the civilian-nuclear-activity waivers completely, while others in the State and Treasury Departments have apparently expressed concern that doing so would threaten non-proliferation efforts.[19] In any event, the Trump administration's decision here represents a continued chipping away at Iran's benefits under the JCPOA.

Iran's Announced Partial Withdrawal from the JCPOA

On May 8, while still expressing a commitment to the JCPOA, Iranian President Rouhani announced that Iran would immediately stop complying with the JCPOA's limits placed on the domestic build-up of enriched uranium and heavy water.[20] (Indeed, those limits became harder to adhere to once the Trump administration revoked waivers allowing Iran to store or sell off these materials.) Further, he declared that Iran would suspend compliance with other parts of the JCPOA if its signatories—the United Kingdom, France, Germany, China, and Russia—do not deliver on the economic benefits promised under the JCPOA. In particular, Rouhani stated he expected the sanctions relief for the oil and banking sectors agreed under the JCPOA to materialize, the two areas hit hardest by U.S. sanctions.

For their part, the JCPOA signatories appear to be taking a wait-and-see approach. In a joint statement, the United Kingdom, France, Germany, and the European Union strongly urged Iran to continue to fully comply with the JCPOA and assured them that legitimate trade with Iran remains a priority, citing the operationalization of "INSTEX"—the special purpose vehicle created in January 2019 to facilitate barter-based trade with Iran.[21] In the same statement, the European nations also expressed "regret" that the United States had re-imposed sanctions following their withdrawal from the deal, and called for non-signatories to refrain from taking actions that undercut the JCPOA.[22] It would seem that the JCPOA signatories have treated Iran's May 8 announcement as a statement of intent—as opposed to an immediate violation of the deal—and thus have refrained from retaliatory action. We will, of course, monitor this situation closely as we approach the 60-day deadline imposed by Rouhani.

New Sanctions on Iron, Steel, Aluminum, and Copper

On May 8, hours after Iran's announcement, President Trump signed an executive order authorizing new sanctions relating to the iron, steel, aluminum, and copper sectors of the Iranian economy.[23] To summarize broadly, blocking sanctions can now be placed on any person who has (1) operated in those sectors; (2) knowingly engaged in a "significant" transaction in those sectors (covered transactions include, among other things, sales, transportation, and marketing); (3) materially supported a person blocked under these sanctions; or (4) been owned or controlled by, or has acted on behalf of, a person blocked under these sanctions. The new industrial-metals sanctions build upon existing sanctions on "raw and semi-finished metals," which include aluminum and steel.[24] Per the May 8 executive order, there will be a wind-down period of 90 days for existing transactions that would violate the industrial-metals sanctions. Any new business activity in the relevant sectors, however, is immediately sanctionable.

Industrial metals account for approximately 10% of Iran's export economy. These sanctions will likely help deepen Iran's economic recession; the country is currently struggling with skyrocketing inflation, rising unemployment, and a currency plummeting in value. Given that the United States shows no signs of letting up its "maximum pressure campaign," we are likely to see more sanctions on Iran and, at the same time, more pushback from Iran on its obligations under the JCPOA.

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[1] The White House, Statement from President Donald J. Trump Regarding Imposing Sanctions with Respect to the Iron, Steel, Aluminum, and Copper Sectors of Iran (May 8, 2019), available at https://www.whitehouse.gov/briefings-statements/statement-president-donald-j-trump-regarding-imposing-sanctions-respect-iron-steel-aluminum-copper-sectors-iran/.

[2] Bill Chappell, U.S. Labels Iran's Revolutionary Guard As A Foreign Terrorist Organization, NPR (Apr. 8, 2019), available at https://www.npr.org/2019/04/08/710987393/u-s-labels-irans-revolutionary-guard-as-a-foreign-terrorist-organization.

[3] *See* U.S. Dep't of State, Fact Sheet, Terrorism Designation FAQs (Feb. 27, 2019), available at https://www.state.gov/r/pa/prs/ps/2018/02/278882.htm.

[4] *See* 18 U.S.C. §§ 2339A, 2339B.

[5] Karen DeYoung, Defense, intelligence officials caution White House on terrorist designation for Iran's Revolutionary Guard, The Washington Post (Feb. 8, 2017), available at https://www.washingtonpost.com/world/national-security/defense-intelligence-officials-caution-white-house-on-terrorist-designation-for-irans-revolutionary-guards/2017/02/08/228a6e4a-ee28-11e6-b4ff-ac2cf509efe5_story.html.

[6] For the statutory basis for those waivers, please see Section 1245(d)(4)(D) of the National Defense Authorization Act for Fiscal Year 2012 (NDAA, P.L. 112-81, signed on Dec. 31, 2011) (22 U.S.C. 8513a).

[7] Ian Talley & Courtney McBride, U.S. to Issue Eight Waivers for Oil Countries Under Iran Sanctions, Wall Street Journal (Nov. 2, 2018), available at https://www.wsj.com/articles/u-s-to-issue-eight-waivers-for-oil-countries-under-iran-sanctions-1541172994.

[8] Press Release, U.S. Dep't of State, Decision on Imports of Iranian Oil (Apr. 22, 2019), available at https://www.state.gov/secretary/remarks/2019/04/291272.htm.

[9] Jessica Donati, U.S. to End Iran Oil Waivers to Drive Tehran's Exports to Zero, Wall Street Journal (Apr. 22, 2019), available at https://www.wsj.com/articles/u-s-to-end-iran-oil-waivers-to-drive-tehrans-exports-to-zero-11555898664.

[10] Press Release, U.S. Dep't of State, Decision on Imports of Iranian Oil (Apr. 22, 2019). Given the likely effect that this recent announcement will have on oil prices, analysts predict that secondary sanctions relating to the import of Venezuelan oil will likely be delayed. *See, e.g.*, S&P Global Platts, End of Iran waivers likely to postpone Venezuela secondary oil sanctions: analysts (Apr. 22, 2019), available at https://www.spglobal.com/platts/en/market-insights/latest-news/oil/042219-end-of-iran-waivers-likely-to-postpone-venezuela-secondary-oil-sanctions-analysts.

[11] Edward Wong & Clifford Krauss, U.S. to Clamp Down on Iranian Oil Sales, Risking Rise in Gasoline Prices, N.Y. Times (Apr. 21, 2019), available at https://www.nytimes.com/2019/04/21/us/politics/us-iran-oil-sanctions.html.

[12] *Id.*; Jessica Donati, U.S. to End Iran Oil Waivers to Drive Tehran's Exports to Zero, Wall Street Journal (Apr. 22, 2019).

[13] Associated Press, China tells US to avoid 'wrong moves' over Iran oil controls (Apr. 24, 2019), available at https://www.seattletimes.com/business/china-tells-us-to-avoid-wrong-moves-over-iran-oil-controls/.

[14] Rishi Iyengar, China buys a lot of Iranian oil, and it's not happy at all with US sanctions, CNN (Apr. 23, 2019), available at https://www.cnn.com/2019/04/22/energy/china-iran-oil-us-sanctions/index.html.

[15] Matthew Lee, U.S. Says No More Sanctions Waivers for Importing Iranian Oil, Real Clear Politics (Apr. 23, 2019), available here.

[16] Chen Aizhu & Florence Tan, Boxed in: $1 billion of Iranian crude sits at China's Dalian port, Reuters (Apr. 30, 2019), available at https://www.reuters.com/article/us-china-iran-oil-sanctions/boxed-in-1-billion-of-iranian-crude-sits-at-chinas-dalian-port-idUSKCN1S60HS.

[17] Humeyra Pamuk & Timothy Gardner, U.S. renews Iran sanctions, grants oil waivers to China, seven others, Reuters (Nov. 5, 2018), available here.

[18] U.S. Dep't of State, Fact Sheet, Advancing the Maximum Pressure Campaign by Restricting Iran's Nuclear Activities (May 3, 2019), available at https://www.state.gov/r/pa/prs/ps/2019/05/291483.htm.

[19] Nicole Gaouette & Jennifer Hansler, US extends nuclear waivers for Iran, but with limits (May 3, 2019), available at https://www.cnn.com/2019/05/03/politics/us-iran-nuclear-waivers/index.html.

[20] BBC News, Iran nuclear deal: Trump raises pressure with sanctions on metals (May 8, 2019), available at https://www.bbc.com/news/world-middle-east-48204646; EU urges Iran to back down from nuclear escalation (May 8, 2019), available at https://euobserver.com/foreign/144864

[21] European Union, Joint statement by High Representative of the European Union and the Foreign Ministers of France, Germany and the United Kingdom on the JCPoA (May 9, 2019), available at https://eeas.europa.eu/headquarters/headquarters-homepage/62093/joint-statement-high-representative-european-union-and-foreign-ministers-france-germany-and_en.

[22] *Id.*

[23] Executive Order Imposing Sanctions with Respect to the Iron, Steel, Aluminum, and Copper Sectors of Iran of May 8, 2019, available at https://www.treasury.gov/resource-center/sanctions/Programs/Documents/iran_eo_metals.pdf.

[24] U.S. Dep't of Treasury, Frequently Asked Questions Regarding Executive Order (E.O.) Imposing Sanctions with Respect to the Iron, Steel, Aluminum, and Copper Sectors of Iran of May 8, 2019, available at https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_iran.aspx#eo_metals.

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The following Gibson Dunn lawyers assisted in preparing this client update: Judith Alison Lee, Adam M. Smith, Christopher Timura, Stephanie Connor, Richard Roeder and Audi Syarief.

Gibson Dunn's lawyers are available to assist in addressing any questions you may have regarding the above developments. Please contact the Gibson Dunn lawyer with whom you usually work, the authors, or any of the following leaders and members of the firm's International Trade practice group:

United States:
Judith Alison Lee - Co-Chair, International Trade Practice, Washington, D.C. (+1 202-887-3591, jalee@gibsondunn.com)
Ronald Kirk - Co-Chair, International Trade Practice, Dallas (+1 214-698-3295, rkirk@gibsondunn.com)
M. Kendall Day - Washington, D.C. (+1 202-955-8220, kday@gibsondunn.com)
Jose W. Fernandez - New York (+1 212-351-2376, jfernandez@gibsondunn.com)
Marcellus A. McRae - Los Angeles (+1 213-229-7675, mmcrae@gibsondunn.com)
Adam M. Smith - Washington, D.C. (+1 202-887-3547, asmith@gibsondunn.com)
Christopher T. Timura - Washington, D.C. (+1 202-887-3690, ctimura@gibsondunn.com)
Ben K. Belair - Washington, D.C. (+1 202-887-3743, bbelair@gibsondunn.com)
Courtney M. Brown - Washington, D.C. (+1 202-955-8685, cmbrown@gibsondunn.com)
Laura R. Cole - Washington, D.C. (+1 202-887-3787, lcole@gibsondunn.com)
Stephanie L. Connor - Washington, D.C. (+1 202-955-8586, sconnor@gibsondunn.com)
Henry C. Phillips - Washington, D.C. (+1 202-955-8535, hphillips@gibsondunn.com)
R.L. Pratt - Washington, D.C. (+1 202-887-3785, rpratt@gibsondunn.com)
Audi K. Syarief - Washington, D.C. (+1 202-955-8266, asyarief@gibsondunn.com)
Scott R. Toussaint - Palo Alto (+1 650-849-5320, stoussaint@gibsondunn.com)

Europe:
Peter Alexiadis - Brussels (+32 2 554 72 00, palexiadis@gibsondunn.com)
Attila Borsos - Brussels (+32 2 554 72 10, aborsos@gibsondunn.com)
Patrick Doris - London (+44 (0)207 071 4276, pdoris@gibsondunn.com)
Sacha Harber-Kelly - London (+44 20 7071 4205, sharber-kelly@gibsondunn.com)
Penny Madden - London (+44 (0)20 7071 4226, pmadden@gibsondunn.com)
Steve Melrose - London (+44 (0)20 7071 4219, smelrose@gibsondunn.com)
Benno Schwarz - Munich (+49 89 189 33 110, bschwarz@gibsondunn.com)
Michael Walther - Munich (+49 89 189 33-180, mwalther@gibsondunn.com)
Richard W. Roeder - Munich (+49 89 189 33-160, rroeder@gibsondunn.com)