

New UK Sanctions on Iran - The Financial Restrictions (Iran) Order 2011

The most recent in a string of sanctions measures focussed on regimes in the Middle East entered into force in the United Kingdom at 3:00 pm on Monday 21 November 2011 in the form of the Financial Restrictions (Iran) Order 2011 (the "Order"). The Order prohibits UK financial and credit institutions from entering into or continuing to participate in any transaction or business relationship with any bank incorporated in Iran, including such banks' branches and subsidiaries (wherever located), and the Central Bank of Iran, unless licensed to do so by HM Treasury.

The Order - a unilateral measure adopted by the United Kingdom - adds a further layer to existing UN and EU mandated sanctions against Iran that bind UK-based institutions and adds to the increasingly onerous compliance challenges facing the financial sector. While many UK-based banks have already severely curtailed or ended relationships involving Iran and its banks in light of existing sanctions in Europe and the extraterritorial gaze of the US authorities, the Order will nevertheless have a significant compliance impact. Importantly, the Order is distinct from the asset-freezing sanctions regime adopted pursuant to UN Security Council resolutions and EU action in pursuit of its Common Foreign and Security Policy.

Basis for the Order

The Financial Restrictions (Iran) Order 2011 is made pursuant to Schedule 7 of the Counter-Terrorism Act 2008 (the "Act"), which empowers the Treasury to give directions if certain conditions are met. In a

Ministerial Statement issued on 21 November, the Financial Secretary to the Treasury justified the Order by reference to Iranian activity facilitating the development or production of nuclear weapons which the government has concluded poses a significant risk to the national interests of the United Kingdom. The announcement referred to concerns raised by the most recent report of the International Atomic Energy Agency (IAEA) that Iran has carried out activities relevant to the development of a nuclear explosive device. The rationale for a direction applying to all Iranian banks is that they play a crucial role in providing financial services that support Iran's proliferation activities; and existing sanctions targeting individual banks have proven insufficient in cutting off this support. The Ministerial Statement also referred to a recent communication from the FATF calling on countries to implement effective measures to protect their financial sectors from money laundering and financing of terrorism risks emanating from Iran.

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Entry into force and Duration

The Order entered into force at 3:00 pm on 21 November 2011. It must be approved by a resolution of each House of Parliament within 28 days in

order to have continuing effect. Assuming that approval is forthcoming, the Order will remain in force for one year unless revoked earlier.

Application of the Order

The Order itself contains only four Articles but, to be understood fully, needs to be read in conjunction with Schedule 7 of the Act. Article 4 of the Order contains a direction that a "relevant person" must not enter into or continue to participate in, any transaction or business relationship with a "designated person". A "relevant person" is, in summary, any person operating in the UK financial sector as a financial or credit institution and all branches of such persons, wherever located. "Designated persons" are, in summary, all banks incorporated in Iran, all subsidiaries and branches of such banks (wherever located) and the Central Bank of Iran.

The term "business relationship" is defined in Schedule 7 of the Act as a business, professional or commercial relationship between a relevant person and a customer, which is expected by the relevant person, at the time when contact is established, to have an element of duration. The term "transaction" is not defined.

HM Treasury Guidance

HM Treasury has issued a Notice providing an explanation of the restrictions, which should be read in conjunction with the Order. Financial institutions can better protect themselves against allegations of non-compliance with the Order if they can demonstrate efforts to adhere to

relevant published guidance (see further, below).

The Notice emphasises that existing business relationships should cease immediately in order to comply with the Direction, and that transactions may not be initiated or completed, unless permitted to continue under one of six general licences. Chapter 5 of the Notice helpfully describes the interaction between the Order and existing financial sanctions in place against Iran. It emphasises that the asset freeze does not conflict with the requirements of the Order; but that the Order prohibits certain activities that are permitted under the existing sanctions. The Notice goes on to clarify that if a new application is made for a license under one regime, then insofar as relevant, it may be taken as applying also to the other.

While the Notice emphasises that it is unlikely that the Treasury will be willing to licence new relationships or business with Iranian banks going forward, the six general licences issued on 21 November permit the following:

- Transactions under €40,000 related to humanitarian activities or purposes, including the export of medical equipment or foodstuffs and the provision of healthcare.
- Transactions under €40,000 for or related to personal remittances.
- Transactions in relation to the provision of insurance which is permitted under Article 26(2) and (3) of EU Regulation 961/2010 against Iran.
- Holding of asset-frozen Iranian banks' accounts.
- Holding accounts of non-frozen Iranian banks.
- Completion by 28 November 2011 of payments to or from

Iranian banks where instructions in relation to the payment had been given at the time of the Order coming into force

HM Treasury and the Export Control Organisation (part of the Department for Business, Innovation and Skills) have noted that the Order may make it difficult for UK companies to trade with Iranian companies who have a banking relationship with an Iranian bank. In particular, UK exporters will no longer be able to use UK credit or financial institutions to make or receive payments to or from Iranian banks, and their banks will be unable to enter into letter of credit arrangements with Iranian banks, unless licensed by HM Treasury.

Offences and Penalties

Breach of the Order is an offence and may result in criminal or civil penalties (although not both). The FSA has power to enforce the Order and impose civil penalties. A penalty may not be imposed (nor will an offence be committed) if a person took all reasonable steps and exercised all due diligence to ensure that the requirements of the direction were complied with if, having done so, the person did not know or have reasonable cause to suspect that activity was prohibited. In deciding whether a firm has committed an offence, a relevant consideration will be whether the firm had followed any relevant guidance available at the time in connection with compliance. The Notice in Chapter 8 therefore emphasises that relevant persons should have policies and procedures in place to ensure compliance with the Order, and directs reference to Treasury approved guidance issued by the Joint Money Laundering Steering Group.

It should be noted that officers of corporate entities may be personally liable when a firm commits an offence if they can be shown to have connived in the relevant corporation's offence, or if the offence was attributable to the officer's neglect.

Other countries' measures

The Order was enacted by HM Treasury on the same day as measures were also adopted in both the United States and Canada as part of a concerted effort to ratchet up pressure on Iran's alleged nuclear ambitions.

Among other measures, the US has designated Iran as a jurisdiction of "primary money laundering concern" under Section 311 of the USA PATRIOT Act. The effect is that US financial institutions are now required to perform additional due diligence to ensure that correspondent banking relationships they maintain are not used to provide Iranian banks with indirect access to the US financial system. While the impact of this is not likely to be felt strongly given that US financial institutions have long been subject to sanctions regulations prohibiting the provision of correspondent account services for banking institutions in Iran, the

measures taken are part of a way of further pressurising non-US banks from engaging in any business with Iran.

Additional measures are also expected to be announced in Europe in the coming days.

As long as the current international tensions remain, this latest round of sanctions is unlikely to be the last.

This Client briefing does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

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