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EU Responds to the Snap-Back of US Sanctions Against Iran: Between a Rock and a Hard Place

In light of the EU's recent amendments to its long-standing blocking measure, EU operators will need to weigh the consequences of failing to comply with their contradicting obligations under US and EU law.

How has the EU responded?

The updated EU Blocking Statute (Council Regulation (EC) No 2271/96) came into force on August 7, 2018, when the EU Commission (the Commission) adopted Commission Delegated Regulation (EU) 2018/1100 amending the Annex to the Blocking Statute.

The Blocking Statute (a) prohibits persons operating within the EU (so-called "EU operators") from complying with certain extra-territorial US sanctions listed in the Annex to the Blocking Statute (US sanctions),[1] (b) allows such persons to recover damages arising from the effects of the US sanctions, and (c) renders foreign court rulings based on the US sanctions invalid within the EU. The amended Blocking Statute is effective as of August 7, 2018, and does not include grandfathering provisions for contractual obligations entered into before that date.

The Commission has also released a Question & Answer style Guidance Note on the Blocking Statute and has adopted Commission Implementing Regulation (EU) 2018/1101 (the Implementing Regulation), which sets out the criteria for EU operators that elect to apply for an authorization from the Commission to comply with the US sanctions and be excepted from Article 5 of the Blocking Statute.

Who does the Blocking Statute target?

In the Guidance Note, the Commission refers to the Blocking Statute applying to "EU operators," which are those persons set out in Article 11 of the Blocking Statute, including:

- Any natural person being a resident in the Union and a national of a Member State;
- Any legal person incorporated within the Union;

- Any national of a Member State established outside the Union and any shipping company established outside the Union and controlled by nationals of a Member State, if the company's vessels are registered in that Member State in accordance with its legislation;

- Any other natural person being a resident in the Union, unless that person is in the country of which he or she is a national; and

- Any other natural person within the Union, including the Union's territorial waters and air space and in any aircraft or on any vessel under the jurisdiction or control of a Member State, acting in a professional capacity.

Q&A 21 of Guidance Note also clarifies that the Blocking Statute applies to EU-based subsidiaries of US companies, but does not apply to branches of US companies in the EU or US subsidiaries of EU companies.

How does the Blocking Statute work?

The Blocking Statute uses four mechanisms to counteract the US sanctions:

- **Notification requirement (Article 2):** EU operators must inform the Commission within 30 calendar days of obtaining information that their economic or financial interests are affected by the US sanctions set out in the Annex. For companies, this obligation applies to their "directors, managers and other persons with management responsibilities."

- **Non-recognition of foreign judgments giving effect to the laws set out in the Annex (Article 4):** No judgment of a court or tribunal located outside the EU giving effect to the US sanctions set out in the Annex may be enforced by the courts of an EU Member State.

- **Prohibition on compliance with the laws set out in the Annex (Article 5):** EU operators are prohibited from complying with the US sanctions set out in the Annex, "whether directly or through a subsidiary or other intermediary person, actively or by deliberate omission." The prohibition extends to "requests of foreign courts, based on or resulting, directly or indirectly, from the laws specified in the Annex or from actions based thereon or resulting therefrom."

  Q&A 5 of the Guidance Note clarifies that the purpose of this prohibition is to ensure that EU operators do not make their business decisions relating to Iran and Cuba by reference to the US sanctions. However, EU operators are free to decide "whether to start working, continue, or cease business operations in Iran or Cuba, and whether to engage or not in an economic sector on the basis of their assessment of the economic situation."

  As discussed further below, EU operators can obtain authorization to comply with the US sanctions, if non-compliance would seriously damage their interests or those of the EU.

- **Claw-back / damages provision (Article 6):** EU operators are entitled to recover damages for losses that they suffer as a result of the application of the laws set out in the Annex.

  Q&A 12 and 13 of the Guidance Note observe that Article 6 is drafted in deliberately broad terms. Article 6 does not provide a conceptual limit on either the damage that can be claimed through court proceedings, or the potential defendants that can be sued (which include not only the persons and entities "causing" the damage, but also their "representatives"). The Guidance Note does not deal

with the possibility of US parties being sued by EU operators in the courts of EU Member States, but the language of Article 6 does not rule out this possibility. The only obvious limiting factor for Article 6 claims appears to be "causation." The relevant court would need to consider whether the link between the action taken as a result of the US sanctions was sufficiently connected to the damage alleged to have been suffered.

Article 6 creates considerable scope for civil litigation (a point emphasized by financial institutions in a recent paper published by UK Finance on July 11, 2018, just prior to the latest updates to the Blocking Statute). Precisely how Article 6 will play out in practice remains to be seen.

Q&A 13 of the Guidance Note poses, but does not answer, the question of whether EU operators "can sue the US authorities." However, Q&A 15 notes that EU Regulation No 1215/2012 (the Brussels Regulation), which governs jurisdiction and the enforcement of judgments within the EU and is referenced in Article 6, only applies to civil and commercial matters, and "does not extend to the liability of the State for acts and omissions in the exercise of State authority." The reference to the Brussels Regulation as applying to Article 6 claims suggests that sovereign immunity restrictions would prevent EU operators from bringing claims against the US governmental authorities unless the latter were acting in a commercial capacity.

Can EU operators comply with competing obligations?

The Implementing Regulation sets out the procedure by which EU operators can apply under Article 5 of the Blocking Statute for an authorization from the Commission to enable them to comply with the US sanctions.

Article 3 of the Implementing Regulation requires any application to:

- explain the provisions of the US sanctions with which the applicant argues it must comply;
- provide the scope of the authorization sought; and
- demonstrate, with evidence, that compliance would cause serious damage to either an EU operator, the interests of the EU, or both.

The Commission's assessment of the application is to be based upon an indicative list of 15 factors set out in Article 4 of the Implementing Regulation. These factors are non-cumulative. The following factors are worth highlighting:

> "the existence of a substantial connecting link with the third country which is at the origin of the listed extraterritorial legislation or the subsequent actions; for example the applicant has parent companies or subsidiaries, or participation of natural or legal persons subject to the primary jurisdiction of the third country which is at the origin of the listed extra-territorial legislation or the subsequent actions."

This criterion suggests that EU subsidiaries owned by US parent companies, EU companies with substantial operations in the US, or EU companies that employ a substantial number of US persons, might find that the Commission looks more favorably on their request for an authorization than a request from a company with limited US links.

> "the adverse effect on the conduct of economic activity, in particular whether the applicant would face significant economic losses, which could for example threaten its viability or pose a serious risk of bankruptcy."

This criterion suggests that the Commission will set a high bar in determining whether an applicant has demonstrated that compliance with the Blocking Statute will cause it serious harm. Q&A 15 of the Guidance Note observes that the authorization procedure is not to be used for "every nuisance or damage suffered by EU operators."

The Commission has also released a Template Application form to be used by EU operators requesting an authorization under Article 5 of the Blocking Statute. Q&A 16 of the Guidance Note observes that the authorization procedure is not to be used as a means of seeking informal guidance from the Commission or "confirmation that [an EU operator's] business decisions are in line with the Blocking Statute."

What are the penalties?

Under EU law, the Blocking Statute has direct legal effect in all EU Member States. The Blocking Statute does not, however, set out any penalties for breach of its provisions, which requires each Member State to pass implementing legislation determining the penalties to be imposed, which must be "effective, proportional and dissuasive."

For instance, the UK implemented the original Blocking Statute in 1996 through the Extraterritorial US Legislation (Sanctions against Cuba, Iran and Libya) (Protection of Trading Interests) Order. An EU person within the territorial jurisdiction of the English courts that breaches the notification requirement or the prohibition on complying with the laws in the Annex to the Blocking Statute in breach of this order is liable to a fine of up to £5,000 upon summary conviction, or an unlimited fine upon conviction on indictment.

What are the risks?

To date, Member States throughout the EU have rarely enforced the Blocking Statute, while the principal US regulator (the Treasury Department's Office of Foreign Assets Control (OFAC)) has aggressively enforced US sanctions compliance. Q&A 8 of the Guidance Note explains that, historically, the Blocking Statute has rarely been enforced as the US granted the EU an exemption from certain provisions of the US sanctions against Cuba. Indeed, some Member States have not actually passed implementing legislation imposing penalties for breaching the Blocking Statute.

We are aware of only one reported case of an EU-incorporated company being prosecuted for complying with the Cuba-related provisions of the Blocking Statute. In April 2007, Austrian authorities brought enforcement action in respect of the reported closure of accounts held by Cuban nationals. Reports suggest that closing these Cuba-linked accounts was required to comply with US sanctions because the entity concerned was to be acquired by a US private equity firm. Following the commencement of the enforcement action in Austria, OFAC reportedly granted the entity a license to re-open the Cuban accounts, and the Austrian authorities dropped the case.

The approach adopted (*i.e*. obtaining an OFAC license to authorize conduct that would otherwise breach the US sanctions) will not now be open to EU operators. Q&A 23 of the Guidance Note states that: "[r]equesting from the U.S. authorities an individual license granting a derogation/exemption from the listed extra-territorial legislation would amount to complying with the latter." [2]

What does the Blocking Statute mean for EU operators?

The updates to the Annex of the Blocking Statute and the new guidance on its operation significantly up the ante in terms of the EU's position on US efforts to enforce sanctions against Iran outside US borders (Cuba likely remains a sideshow for this purpose). EU operators will now need to weigh the consequences of complying with US secondary sanctions against Iran against competing obligations under the Blocking Statute.

Endnotes

1 a) The Cuban Liberty and Democratic Solidarity Act of 1996
b) The Iran Sanctions Act of 1996
c) The Iran Freedom and Counter-Proliferation Act of 1996
d) The National Defense Authorization Act for Fiscal Year 2012
e) The Iran Threat Reduction and Syria Human Rights Act of 2012
f) The Iranian Transactions and Sanctions Regulations

This list includes OFAC's primary sanctions (the Iranian Transactions and Sanctions Regulations) and US secondary sanctions.

2 Q&A 23 does still permit EU operators to apply for an OFAC license if they have first received an authorization to do so from the Commission under Article 5 of the Blocking Statute. Furthermore, EU operators are permitted to liaise with OFAC and the US authorities to discuss the effect of US sanctions on their business without first obtaining an authorization. Q&A 23 suggest that the Commission will consider it natural for EU operators to have engaged with OFAC before applying for an authorization under Article 5, as the dialogue with OFAC will enable the applicant to narrow down the scope and effect of the relevant US sanctions, and so make a more focused request for authorization.

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