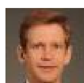
Will the Obama Administration Implement the Stringent Sanctions Authorized Under the Iran Agreement?

by Patrick Clawson **(/experts/patrick-clawson)**

Aug 21, 2015
Also available in
العربية (/ar/policy-analysis/hl-stnfwdh-adart-awbama-alqwbat-alsarmt-almsmwh-bha-bmwjb-alatfaq-m-ayran)

ABOUT THE AUTHORS



Patrick Clawson (/experts/patrick-clawson)
Patrick Clawson is Morningstar senior fellow and director of research at the Washington Institute for Near East Policy.

Brief Analysis

Even after the deal is in effect, the United States can sustain or increase tough barriers on Iran's trade with other countries, but this fact has not been highlighted by the president or his team.

On August 19, in a move designed to address concerns by wavering members of Congress, President Barack Obama sent a letter to Rep. Jerrold Nadler (D-NY) outlining some steps his administration will take after the nuclear deal's implementation to continue to press Iran. Another set of clarifications the administration could issue toward the same end would be about the sanctions pressure Washington will apply to block Iran from normal trading relations with other countries.

Indeed, under the nuclear deal Washington has reserved rights to preserve serious limits on Iranian trade with European and Asian firms. However, it is by no means clear if the Obama administration will make vigorous use of those rights. Sanctions are never automatic: just because the U.S. government has the authority to block certain transactions does not mean it will actively make use of that power, including through vigorous enforcement. At least some of those uncertain about the nuclear deal would feel more comfortable were there convincing evidence that the administration plans to continue vigorously impeding normal Iranian trade.

The potential barriers fall into several categories: sanctioning foreign banks involved in Iran trade, supporting seizure of Iranian assets, highlighting the risks from Iranian deceptive financial practices, and maintaining regulatory pressure.

Continuing U.S. Sanctions on Foreign Banks Involved in Iran Trade

At present, the 2010 Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA) prohibits U.S. banks from opening or maintaining correspondent or payable-through accounts for any foreign financial institutions that fall afoul of its provisions, effectively shutting these institutions off not only from the U.S. banking system but from all transactions in U.S. dollars. This has been a serious impediment to normal Iranian trade. Asian firms, among others, have faced complications arranging for payment as a result.

In the Joint Comprehensive Plan of Action's (JCPOA's) Annex II.B.4.1.1, Washington pledges to "cease the application" of certain sanctions, but this applies only to Section 104(c)(2)E(ii)(I), one small provision of CISADA. Nothing is said in the JCPOA about the rest of CISADA. Namely, the other parts of Section 104(c)(2) of CISADA describe a wide range of activities that can justify U.S. sanctions on a foreign financial institution. Such activities include if the institution "facilitates the efforts of the Government of Iran (including efforts of Iran's Revolutionary Guard Corps or any of its agents or affiliates)...to provide support for organizations designated as foreign terrorist organizations"; "engages in money laundering" to that end; "facilitates efforts by the Central Bank of Iran [CBI] or any other Iranian financial institution" to that end; or "provides significant financial services for Iran's Revolutionary Guard Corps [IRGC] or any of its agents or affiliates whose property or interests in property are blocked pursuant to the International Emergency Economic Powers Act" or for "a financial institution whose property or interests in property are blocked pursuant to that Act in connection with...Iran's support for international terrorism."

The list of activities subjecting foreign banks to the secondary CISADA sanctions is potentially far-reaching. Many IRGC "agents or affiliates," such as Iran's largest construction company, Khatam al-Anbia, and the IRGC's retirement funds and credit unions, are major economic actors, and arguably any dealings with them constitute facilitating efforts to support terrorist organizations. As then treasury secretary Timothy Geithner said in 2011 when designating "the entire Iranian banking sector -- including the Central Bank of Iran -- as a threat" under Section 311 of the USA PATRIOT Act, "If you are a financial institution and you engage in any transaction involving Iran's Central Bank or any other Iranian bank operating inside or outside Iran, you are at risk of supporting Iran's illicit activities: its pursuit of nuclear weapons, its support for terrorism, and its efforts to deceive responsible financial institutions and evade sanctions. Any and every financial transaction with Iran poses grave risk of supporting those activities." This language would suggest that the CISADA provisions could be easily triggered if a foreign bank has dealings with an Iranian bank.

The JCPOA is less than clear about what sanctions remain. For instance, Annex II.7.2. gives a long list of activities banks may carry out post-implementation, but footnote 14 specifies that "the sanctions lifting described in this Section...is without prejudice to sanctions that may apply under legal provisions other than those cited in Section 4" -- in other words, the CISADA provisions still apply. Indeed, Annex 2, Attachment 3, of the JCPOA provides a long list of Iranian institutions no longer subject to sanctions under various provisions. This list, however, is distinct from any decision about whether CISADA's provisions still apply to such institutions; that is, those institutions may still be subject to extensive sanctions even though they will no longer be penalized for proliferation activities.

Billions in Court Judgments

Another barrier to Iran resuming normal foreign trade with Europe and Asia could be the vigorous legal actions planned by private U.S. lawyers and plaintiffs aimed at seizing Iranian assets linked to U.S. court judgments against Iran and its instrumentalities for supporting terrorist attacks against specific Americans. (Full disclosure: this writer has been an expert witness in many such cases.) Those judgments now total $46 billion. A case the Supreme Court is considering taking involves about a billion dollars transiting U.S. banks while en route between non-U.S. banks and destined for the CBI. Those funds were frozen and judged by the U.S. Second Court of Appeals in New York to be liable to seizure. The lawyers and plaintiffs involved are quite determined to pursue any Iranian funds that may be cleared through New York-based banks, which could complicate the use of U.S. dollars in Iran's

trade.

The New York case was facilitated considerably by the Obama administration's tipping off the lawyers seeking the funds. Were it or the next administration to similarly cooperate with lawyers seeking to enforce U.S. court judgments, foreign financial institutions dealing with Iran could still face vigorous legal actions. Nothing in the JCPOA forecloses this possibility.

Highlighting Iranian Deceptive Practices

As noted above, since 2011 all Iranian financial institutions have been designated under Section 311 of the Patriot Act as being institutions of "primary money laundering concern," which requires U.S.-based financial institutions, including foreign-owned institutions, to take certain "special measures." This designation is about money laundering, not proliferation, and nothing indicates the laundering designation is going away.

Iranian financial institutions have a long history of engaging in multiple deceptive financial practices that flout international norms. Since 2007, the Financial Action Task Force (FATF), a thirty-four-member international organization created in 1989 to establish standards to combat money laundering and terrorism financing, has issued warnings about Iranian practices. Its most recent "Public Statement," of June 26, called "on its members and other jurisdictions to apply counter-measures to protect the international financial system from the on-going and substantial money laundering and terrorist financing (ML/FT) risks emanating from" Iran and North Korea. Foreign banks that ignore the FATF could well find themselves subject to U.S. regulatory scrutiny.

Maintaining Regulatory Pressure

If foreign financial institutions wish to learn exactly what activities they can and cannot engage in with Iranian banks, the U.S. Department of Treasury is not likely to give much satisfaction. The Treasury Department has historically been unwilling to issue legally binding assurances allowing certain activities to proceed, preferring to preserve the right to take legal action against banks in the event fresh information casts new light on particular transactions -- or if the department decides to change its attitude toward those transactions. While at times it has issued what some call "letters of comfort," the vague and nonbinding language actually provides little comfort. Given that major banks such as the French BNP Paribas paid billions in fines for activities they thought U.S. regulators did not then object to but only later regarded as violations, many banks may be reluctant to act based on such letters, even if they were issued.

And this tells only the federal government side of the story. The British Standard Chartered bank faced a serious threat to its New York banking license from New York's Department of Financial Services (DFS) over sanctions violations. At times, the DFS appears to have relished taking a tougher stance than the U.S. Treasury Department. Banks cannot be certain about what the DFS will do about Iran-related transactions. To be sure, paragraph 25 of the JCPOA states, "If a law at the state or local level in the United States is preventing the implementation of the sanctions lifting as specified in this JCPOA, the United States will take appropriate steps, taking into account all available authorities, with a view to achieving such implementation." But this language only encompasses the "sanctions lifting as specified in this JCPOA," rather than actions on the other grounds described above such as money-laundering and terrorism concerns.

After facing tens of billions of dollars in fines for sanctions violations or actions including improper handling of mortgages and manipulating interest rates and foreign exchange rates, many major international banks have adopted "derisking" initiatives to protect themselves. The derisking approach has led many major banks to abandon some lucrative markets. On this count, some may regard Iran as a marginal market at best, especially if Washington shows a strong will to go as far as permitted under the JCPOA. To be sure, Iran will almost certainly find smaller banks with less exposure to U.S. regulators willing to run the risks, such as the Ukrainian and Tunisian banks that

have been handling the trade with Iran newly permitted under the interim nuclear accord. But such smaller banks will face serious challenges handling the volumes of trade finance desired by Iran, and they certainly cannot provide the long-term financing for which Iran is hoping.

How Much Pressure Will Iran Face?

Perhaps the most important barriers Iran will face to attracting more foreign businesses involve the country's own poor business environment, including the rampant corruption, the dysfunctional legal system, the frequent policy changes, and the blurred lines of responsibility that can subject firms to demands from many government actors. While particularly important as impediments to investment, these problems will also affect trade.

That said, U.S. sanctions could also remain an important barrier to normal Iranian trade with any country despite the nuclear deal if the administration were so minded. Some of the barriers Iran will face to normal foreign trade after the deal's implementation have received considerable attention, especially (1) the possibility that UN-EU-U.S. sanctions will snap back in the event of disputes about implementation and (2) the continued ban on nearly all direct trade with the United States. Less attention, however, has gone to the potential for many other continued U.S. sanctions on foreigners trading with Iran, although one exception is a detailed analysis in Tyler Cullis's policy memo from the National Iranian American Council, a strong supporter of the nuclear deal.

Paragraph 26 of the JCPOA states, "The United States will make best efforts in good faith to sustain this JCPOA and to prevent interference with the realisation of the full benefit by Iran of the sanctions lifting specified in Annex II." That carefully crafted sentence only says that Washington will make its best efforts regarding the sanctions lifting specified in Annex II. But Washington's pledges for Annex II sanctions lifting do not include the various issues described above, including secondary sanctions on foreign banks because of Iranian money laundering and support for terrorism.

The Obama administration has provided precious little public explanation of its plans for post-deal-implementation sanctions on banks dealing with Iran. The Obama team's silence in the face of extensive reporting that these sanctions are disappearing suggests that perhaps the sanctions will not be vigorously enforced. The criticism about how much Obama is rewarding Iran would look less plausible if the administration enunciated its plans to maintain these sanctions and, most especially, if it secured statements from European governments acknowledging that this is Washington's intent and is fully consistent with the JCPOA.

To the contrary, Treasury Secretary Jacob Lew has implied that Washington has not secured European buy-in for continued secondary sanctions and does not intend to impose then. In an August 13 *New York Times* op-ed, he wrote, "Imposing powerful secondary sanctions against those that refuse to follow our lead...would be a disaster...If we were to cut them off from the American dollar and our financial system, we would set off extensive financial hemorrhaging, not just in our partner countries but in the United States as well." Lew's statement follows the pattern of treasury secretaries warning of dire consequences for the U.S. economy and the entire international financial system if sanctions are toughened. In 2006, Treasury Secretary Henry Paulson predicted that sanctions on the CBI would wreak havoc on global markets and the U.S. economy. When Geithner's 2010 warnings about comprehensive sanctions on the CBI -- which the Patriot Act designation was meant to forestall -- were overridden by the Senate in a 100-0 vote, the result, according to the Obama administration, was to lead Iran to return to negotiations and to offer concessions. For its part, the executive branch had followed its own pattern of warning about the consequences of sanctions only to trumpet them, once enacted, as a key to accomplishing its objectives. Perhaps this time when the treasury secretary cries wolf, the wolf is indeed at the door -- or perhaps not.

Even if the Obama team does little to retain the pressure on foreign financial institutions, the next U.S. administration could decide to be more proactive. Much could be done within the framework of the JCPOA because

Washington has only pledged to take extremely modest steps. The failure of the Obama administration to clarify the meaning of various provisions -- which on their face appear to provide much sanctions relief but on close reading suggest that need not be the case -- has fed the critics' skepticism about what the Obama team plans to do.

Patrick Clawson is director of research at The Washington Institute. ❖

RECOMMENDED

BRIEF ANALYSIS

Bennett's Bahrain Visit Further Invigorates Israel-Gulf Diplomacy

Feb 14, 2022

◆

Simon Henderson

(/policy-analysis/bennetts-bahrain-visit-further-invigorates-israel-gulf-diplomacy)

BRIEF ANALYSIS

Libya's Renewed Legitimacy Crisis

Feb 14, 2022

◆

Ben Fishman

(/policy-analysis/libyas-renewed-legitimacy-crisis)

BRIEF ANALYSIS

The UAE Formally Ceases to be a Tax-Free Haven

Feb 14, 2022

◆

Sana Quadri,
Hamdullah Baycar
(/policy-analysis/uae-formally-ceases-be-tax-free-haven)

TOPICS

Energy & Economics (/policy-analysis/energy-economics)

U.S. Policy (/policy-analysis/us-policy)

REGIONS & COUNTRIES

Iran (/policy-analysis/iran)