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The EU is Launching "INSTEX" to Support Trade with Iran Despite U.S. Sanctions

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On January 31, 2019—four months after the EU Commission confirmed its intention to adopt specific measures aimed at facilitating trade with Iran and thus mitigating the impact of the snapback of U.S. secondary sanctions on EU companies—the foreign ministers of France, Germany, and the United Kingdom announced, “in accordance with their resolute commitment and continued efforts to preserve the Joint Comprehensive Plan of Action (“JCPOA”),” the creation of INSTEX SAS (*Instrument for Supporting Trade Exchanges*), a Special Purpose Vehicle aimed at facilitating legitimate trade between European economic operators and Iran. INSTEX is financed and managed by France, Germany, and the U.K. (the so called “E3”),¹ and only backed by the EU Commission. In fact, the same day, the High Representative of the EU for Foreign Affairs and Security Policy and Vice-President of the EU Commission, Federica Mogherini, publicly reported the creation of the new instrument as a part of the EU’s efforts to support the JCPOA and trade with Iran.²

Background

On May 8, 2018, President Donald Trump announced that the United States would not sign a 120-day waiver of U.S. sanctions against Iran, effectively withdrawing from JCPOA and re-introducing—after a 90/180 day wind-down period (depending on the sanctions)—all previously lifted sanctions (see our Client Alert of May 9, 2018³). Both the wind-down periods have fully expired, and therefore the full set of sanctions targeting Iran, including the secondary sanctions, are in force again. Recent OFAC enforcement actions suggest that implementation of renewed or expanded sanctions against non-U.S. persons will likely be aggressive, taking advantage of broader theories of extra-territorial liability that have developed in recent years, even for companies with no U.S. operations. In that context the EU Commission announced the adoption of a set of measures intended, on the one hand, to mitigate the impact of U.S. sanctions on EU companies, and on the other hand to maintain the growth of economic relations between the EU and Iran, while safeguarding the relationship and cooperation with the U.S. in many sectors (see our Client Alert of May 29, 2018 for more details⁴). INSTEX is part of this set of measures.

The Scope of INSTEX and the Reactions from the U.S.

According to the very preliminary available information, INSTEX would operate as a Euro-denominated clearing house for Iran to conduct trade with European companies, acting outside the global financial system in an attempt to protect European companies from U.S. sanctions enforcement. It is reported that INSTEX is headquartered in France and headed by Mr. Per Fischer, a former manager at Commerzbank.



In their joint statement, the E3 Foreign Ministers also declared that:

- INSTEX will support legitimate European trade with Iran, focusing initially on the sectors most essential to the Iranian population, such as pharmaceutical, medical devices, and agri-food goods;
- INSTEX aims in the long term to be open to economic operators from third countries who wish to trade with Iran;
- The operationalisation of INSTEX will follow a step-by-step approach: the E3 together with INSTEX will continue to work on concrete and operational details to define the way the company will operate;
- The E3 will also work with Iran to create an effective and transparent corresponding entity that is required to be able to operationalise INSTEX; and
- INSTEX will function under the highest international standards with regards to anti-money laundering, combating the financing of terrorism (AML/CFT), and EU and UN sanctions compliance.

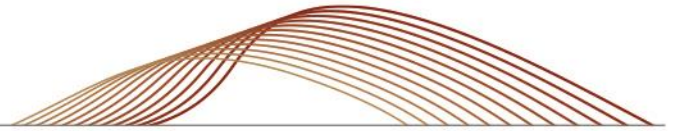
Therefore, at least initially, this new tool will apply only to non-sanctionable essential goods, such as humanitarian, medical, and farm products. The instrument does not address oil-related transactions (which are actually Iran's primary source of foreign currency), thus it will initially have a limited application and a limited impact.

The details of INSTEX and its functioning are not yet available, since the special purpose vehicle is not yet operative and it will also require the creation of a corresponding entity in Iran in order to be operative. Therefore, at this stage, it is more a political declaration than a measure suitable to impact EU-Iran trade, and it is premature to make any evaluation on its actual effectiveness and on the consequences on a broader basis (especially with respect to the relationship with the U.S.). However, it looks like the system is mainly aimed, for the time being, at small and medium-sized EU companies that would provide a small trade volume, while EU multinational companies, and any EU subject with a significant business involving the U.S. market, or dealing with global financial institutions, will likely not change their approach to Iran-related trade due to the high risk deriving from the U.S. sanctions programs.

In this respect, it is reported that the U.S. embassy in Berlin is reassured about the limited impact of such a system, unable—in its view to sensibly impact the “maximum economic pressure campaign” against Iran, and warned European countries, “Entities that continue to engage in sanctionable activity involving Iran risk severe consequences that could include losing access to the U.S. financial system and the ability to do business with the United States or U.S. companies.”⁵

The reported news is another clear sign that the current clash between the U.S. and EU sanctions programs concerning Iran is far from being solved, and a reaction from the U.S. in terms of stricter enforcement of the sanctions also to non-U.S. operators cannot be excluded.

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- ¹ <https://www.gov.uk/government/news/joint-statement-on-the-new-mechanism-to-facilitate-trade-with-iran>.
 - ² https://eeas.europa.eu/headquarters/headquarters-homepage_en/57475/Statement%20by%20High%20Representative/Vice-President%20Federica%20Mogherini%20on%20the%20creation%20of%20INSTEX,%20Instrument%20for%20Supporting%20Trade%20Exchanges.
 - ³ <http://www.paulhastings.com/publications-items/details?id=15fcb66a-2334-6428-811c-ff00004cbded>.
 - ⁴ <https://www.paulhastings.com/publications-items/details?id=5d25e36a-2334-6428-811c-ff00004cbded>.
 - ⁵ Joseph Giordano-Scholz, spokesman of the US embassy in Berlin, reporting the position of President Trump: <https://www.nytimes.com/reuters/2019/01/31/business/31reuters-iran-usa-sanctions-reaction.html>.

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