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January 24, 2012

The Honorable Claire McCaskill
Chairman
Subcommittee on Contracting Oversight
Committee on Homeland Security and Governmental Affairs
United States Senate

Subject: *Actions to Enforce the Iran Sanctions Act and Implement Contractor Certification Requirement*

Dear Madam Chairman:

It is the policy of the United States to deter Iran from developing its nuclear program, supporting terrorism, and abusing human rights by limiting the development of Iran's energy sector, which is vital to its economy and government. The Iran Sanctions Act of 1996 (ISA), as amended, provides for sanctions against firms determined to have made certain investments in Iran's energy sector.¹ While the ISA applies to all firms, U.S. firms were already prohibited from investing in Iran under a U.S. trade embargo, and the ISA was enacted to encourage foreign firms to withdraw from the Iranian market. However, no sanctions have been imposed under the ISA by any prior administration.

The Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010 (CISADA)² amended the ISA by expanding the energy-related activities for which sanctions could be applied to include firms determined to have provided to Iran or invested in Iran's development of refined petroleum products.³ Sanctions include excluding firms from receiving U.S. government contracts. CISADA also directed that the Federal Acquisition Regulation (FAR) be revised to require firms seeking U.S. government contracts to certify that neither they nor any firms owned or controlled by them are engaged in activities for which sanctions may be imposed under section 5 of the ISA. If a contractor submits a false certification, agencies may terminate the contract, or suspend or debar the contractor, in accordance with procedures in the FAR, from government contracts. The certification requirement may be waived in the interest of national security. The Department of State (State) is responsible for enforcing the energy-related sanctions under the ISA, as amended.

¹ Iran and Libya Sanctions Act of 1996, Pub. L. No. 104-172, § 5, 110 Stat. 1541, 1543, as amended. The name of the law was changed to Iran Sanctions Act of 1996 in 2006 by the Iran Freedom Support Act, Pub. L. No. 109-293, 120 Stat. 1344.

² Pub. L. No. 111-195, 124 Stat. 1312.

³ The act provides for sanctions against firms that sell or provide refined petroleum or related goods and services, including technology, information, or support, that could directly and significantly facilitate the maintenance or expansion of Iran's domestic production of refined petroleum products.

In response to your request, this report (1) identifies State actions and processes to enforce energy sector-related sanctions under the ISA and (2) describes the implementation of the contractor certification requirement and identifies any indications of false certifications or the need for waivers of the certification requirements. We are issuing a separate report covering firms identified in open sources as selling refined petroleum products to Iran from July 2010 through December 2011.⁴

To identify State actions and processes to enforce the ISA, we reviewed State announcements of ISA sanctions and subsequent *Federal Register* notices describing the specific sanctions against each firm. We interviewed State officials to document their sources of information and methods used to identify firms engaging in sanctionable activity and searched the Excluded Parties List System (EPLS)⁵ to confirm if sanctioned firms were declared ineligible to receive government contracts. We did not independently determine whether actions were sanctionable under the ISA. To describe the implementation of the contractor certification requirement and identify any indications of false certifications or the need for waivers, we reviewed the rules implementing the requirement and subsequent changes to the FAR and discussed these changes with a senior Office of Federal Procurement Policy official for technical accuracy. We searched the Federal Procurement Data System-Next Generation (FPDS-NG)⁶ and the Central Contractor Registration System⁷ to determine if any of the sanctioned firms held any government contracts or were registered to respond to solicitations after the certification requirement went into effect. We searched under multiple fields, including company, vendor, and contractor name fields using all known firm names and abbreviations. Based on our efforts, we believe the information we obtained is sufficiently reliable for this report.

We conducted this performance audit from September 2011 to January 2012 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

⁴ GAO, *Firms Reported in Open Sources to Have Sold Iran Refined Petroleum Products Declined since June 30, 2010*, [GAO-12-321R](#) (Washington, D.C.: Jan. 24, 2012).

⁵ EPLS is an electronic database containing the list of all parties suspended, proposed for debarment, debarred, declared ineligible, or excluded or disqualified by agencies. It is available for agency and public access at www.epls.gov.

⁶ FPDS-NG is the primary governmentwide contracting database for more than 60 government agencies, departments, and other entities.

⁷ Prospective contractors generally must be registered in the Central Contractor Registration System prior to the award of a contract (FAR subpart 4.11).

Results in Brief

Since the fall of 2010, State has sanctioned 13 foreign firms under the ISA—2 for investments in Iran’s energy sector⁸ and 11 for supplying refined petroleum products.⁹ State imposed various sanctions on each firm, listed 10 in EPLS making them ineligible to receive U.S. government contracts, and was in the process of listing the remaining 3 firms in EPLS at the time of this report. To enforce the ISA, State has increased its staff to review available information on companies’ activities in Iran’s energy sector, including information indicating whether affiliated parent companies should be held accountable, relying heavily on the intelligence community and U.S. embassies to corroborate the information. The final decision on whether to apply sanctions is made by the Secretary of State or a delegatee after the information and evidence of potentially sanctionable activity is vetted through State and other agencies when applicable. In addition to sanctions, State officials told us that they have been successful in persuading firms to end their business dealings with Iran, and that the number of foreign firms involved in Iran’s energy sector has declined. However, they acknowledged that some firms are still operating in Iran’s energy sector, and they are continuing their efforts to enforce the ISA.

In September 2010, the administration revised the FAR, as required by CISADA, to include a requirement for prospective contractors to certify that they or any firm owned or controlled by them are not engaging in activities for which sanctions may be imposed under section 5 of the ISA.¹⁰ The certification was subsequently added to the governmentwide electronic system for maintaining various certifications and representations that are required for contractors to do business with the government. The FAR was also revised to include remedies upon determination of false certification and procedures for obtaining waivers to the certification requirement, which would be needed if it was in the national interest for an agency to contract with a firm that has engaged in sanctionable activity.¹¹ However, none of the 13 firms sanctioned by State under the ISA held government contracts or were registered to respond to solicitations for contracts, or submitted an offer after the certification requirement went into effect, so there is no evidence of false certifications or the need for waivers.

Background

U.S. law restricts U.S. firms from investing in Iran’s energy sector through a variety of sanctions administered by the Department of the Treasury to discourage Iran from supporting terrorism and developing nuclear weapons.¹² Section 5(a) of the ISA, as

⁸ See 75 Fed. Reg. 62916-02 (Oct. 13, 2010) (imposing sanctions on Naftiran Intertrade Company), and 76 Fed. Reg. 18821-04 (Apr. 5, 2011) (imposing sanctions on Belarusneft).

⁹ See Public Notice 7585, 76 Fed. Reg. 56866 (Sept. 14, 2011) (imposing sanctions on Allvale Maritime Inc., Associated Shipbroking, Petrochemical Commercial Company International, Petroleos de Venezuela S.A., Royal Oyster Group, Soci’Et’E Anonyme Mon’Egasque D’Administration Maritime Et A’Erienne, Speedy Ship, and Tanker Pacific Management (Singapore) Pte. Ltd.).

¹⁰ 75 Fed. Reg. 60254 (Sept. 29, 2010).

¹¹ 76 Fed. Reg. 68027-28; FAR § 25.703-2; and FAR § 25.703-4.

¹² International Emergency Economic Powers Act, Pub. L. No. 95-223, 91 Stat. 1625 (1977); National Emergencies Act, Pub. L. No. 94-412, 90 Stat. 1255 (1976); and 3 U.S.C. § 301 as implemented by Executive Order 12957, 60 Fed. Reg. 14615 (Mar. 15, 1995) (prohibiting U.S. involvement with petroleum development in Iran). Also, see Exec. Order No. 12959, 60 Fed. Reg. 24757 (May 6, 1995) (banning specified exports and investment), and Exec. Order No. 13059, 62 Fed. Reg. 44531 (Aug. 19, 1997) (prohibiting virtually all trade and investment activities with Iran by U.S. persons, wherever located).

amended, requires that absent a waiver,¹³ the President impose at least three of nine possible forms of sanctions on persons,¹⁴ including foreign firms, determined in any 12-month period to have made an investment of \$20 million or more that directly and significantly contributes to the enhancement of or Iran's ability to develop its petroleum resources. Sanctions can include barring firms from receiving any U.S. government contracts for goods or services.¹⁵ The President has delegated the authority to impose energy-related sanctions under the ISA to the Secretary of State.¹⁶ State's Office of Terrorism Finance and Economic Sanctions Policy, within its Bureau of Economics and Business Affairs, is primarily responsible for investigating foreign firms and recommending sanctions under the act.

In 2010, CISADA expanded the ISA to require sanctions against firms determined to have provided refined petroleum products to Iran above specified monetary thresholds or certain goods, services, technology, information, or support to Iran related to the importation or development of refined petroleum.¹⁷ While the act applies to all firms, U.S. firms were already prohibited from investing in Iran under a U.S. trade embargo. CISADA also provided for the "Special Rule" that allows an investigation not to be opened or to be terminated when firms are no longer engaging in the activity that was the basis for the investigation or have taken significant verifiable steps toward stopping the activity, and State has received reliable assurances that the firm will not knowingly engage in sanctionable energy-related activity in the future. CISADA also requires that not later than 90 days after enactment, the FAR be revised to require a certification from prospective contractors that they, and any firm owned or controlled by them, do not engage in any activity for which sanctions may be imposed under section 5 of the ISA.¹⁸ The act also provides that if the head of an executive agency determines that a false certification has been submitted after the requirement becomes effective, the head of that agency shall terminate the contract or debar or suspend the firm from eligibility for federal contracts.¹⁹ The certification requirement may be waived if the President determines it is in the national interest of the United States to do so.

State Sanctioned 13 Foreign Firms under the ISA and Relies Heavily on Intelligence Sources in Investigating Firms

In the fall of 2010, State announced the first sanctions under the ISA against Naftiran Intertrade Co., a Switzerland-based international trading company, for its investments in Iran's energy sector. Since then, State has imposed sanctions against 12 additional foreign firms, as shown in table 1. The first 2 firms were sanctioned for investments in Iran's energy sector, and the remaining 11 were sanctioned for actions related to new provisions provided

¹³ Pub. L. No. 104-172, § 9(c), as amended. Other exceptions to the imposition of sanctions can be found at section 5(f) of the ISA.

¹⁴ A "person" is defined as a natural person; corporation, business association, partnership, society, trust, financial institution, insurer, underwriter, guarantor, and any other business organization; any other nongovernmental entity, organization, or group; any governmental entity operating as a business enterprise; and any successor.

¹⁵ Other sanctions include a denial of Export-Import Bank assistance, a ban on issuing licenses to export controlled technologies to the sanctioned firm, limits on loans from United States financial institutions, and a ban on property transactions.

¹⁶ The Department of the Treasury is responsible for implementing certain economic-related sanctions under the ISA as amended by CISADA. Memorandum: Delegation of Certain Functions and Authorities under the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010, 75 Fed. Reg. 67025 (Sept. 23, 2010).

¹⁷ Pub. L. No. 111-195, § 102(a).

¹⁸ Pub. L. No. 111-195, § 102(b).

¹⁹ *Id.*

by CISADA for activity related to supplying refined petroleum products to Iran. State imposed various sanctions on each firm, listed 10 in EPLS making them ineligible to receive U.S. government contracts, and was in the process of listing the remaining 3 firms in EPLS at the time of this report.²⁰

Table 1: Foreign Firms Sanctioned by State under the ISA.

Sanctioned foreign firm	Country	Effective date
1. Naftiran Intertrade Co (NICO)	Switzerland	October 13, 2010
2. Belarusneft	Belarus	April 5, 2011
3. Petrochemical Commercial Company International (PCCI)	Jersey/Iran	May 24, 2011
4. Royal Oyster Group	UAE	May 24, 2011
5. Speedy Ship (SPD)	UAE/Iran	May 24, 2011
6. Associated Shipbroking (SAM)	Monaco	May 24, 2011
7. Petr�leos de Venezuela (PDVSA)	Venezuela	May 24, 2011
8. Tanker Pacific Management	Singapore	May 24, 2011
9. Allvale Maritime, Inc.	Liberia	August 26, 2011
10. Societe Anonyme Monegasque d'Administration Maritime et Aeriennne (SAMAMA)	Monaco	August 26, 2011
11. Zhuhai Zhenrong Co (Zhenrong)	China	January 12, 2012
12. Kuo Oil (S) Pte. Ltd. (Kuo)	Singapore	January 12, 2012
13. FAL Oil Company Ltd. (FAL)	UAE	January 12, 2012

Source: State Department.

State officials told us that the department's Office of Terrorism Finance and Economic Sanctions Policy, which previously had one person working on Iran sanctions issues, now has a five-person Iran Sanctions Team focused on enforcement of energy-related ISA sanctions. They also noted that their actions to enforce the ISA began before the 2010 passage of CISADA, but the act led to a significant increase in State's workload by broadening the range of sanctionable activities, including adding a requirement to review company activities related to the sale of specified amounts of refined petroleum products or the development of Iran's refining capability.

²⁰ As of January 18, 2012, according to State officials, they were in the process of listing Zhenrong, Kuo, and FAL in EPLS.

State officials noted that members of the Iran Sanctions Team collect and evaluate information related to Iran's energy sector and refining capacity from available sources, including press reports; however, these sources often turn out to be false or misleading. As a result, these officials told us that they rely on information from numerous intelligence organizations, including State's Bureau of Intelligence and Research, the Office of the Director of National Intelligence, the Central Intelligence Agency, and the Office of Naval Intelligence. Once State identifies information about a foreign firm's investment or activity in Iran's energy sector, officials stated they request a compilation of intelligence information about the firm, and members of the Iran Sanctions Team then evaluate the information to determine if any of the activity might be sanctionable under the ISA.

State officials noted that because sanctions can have an impact on the foreign firm and possibly affect foreign relations with the country in which the firm is located, it is imperative to corroborate information gathered through the intelligence community and other sources. To do so, officials told us that they often utilize embassy officials in the respective country to engage officials from both the foreign firm and its government. State officials acknowledged that such corroboration can be challenging because the intelligence information is often classified or sensitive and needs to be declassified before it can be shared with foreign governments or foreign firms, which takes additional time.

State officials also told us that whenever they uncover activity that is potentially sanctionable, they attempt to determine if there is an affiliated parent company that should also be held accountable. The ISA provides that a firm that owns or controls another firm engaging in sanctionable activity may also be sanctioned, if it knew or should have known about the activity.²¹ However, officials noted that there are challenges in identifying affiliates that could be sanctioned. Specifically, they noted that identifying relationships, ownership, or control of foreign firms is often difficult, especially for closely held firms where limited information is available. However, State will impose sanctions on a parent company when there is evidence that the company knew, or should have known, about the activity of its affiliate. For example, State officials told us that Societe Anonyme Monegasque D'Administration Maritime Et Aeriennne was sanctioned for the activities of its affiliates—Tanker Pacific Management and Allvale Maritime.

According to State officials, once information about a firm's potentially sanctionable activity has been gathered, evaluated, and corroborated, the Iran Sanctions Team prepares a summary of the evidence of the firm's investments or activity in Iran and circulates it for review at the Deputy Secretary level or higher—and as appropriate, by officials from other agencies, including the Department of the Treasury. State officials added that discussions within State include whether to impose sanctions and what sanctions to apply, with the final decision made by the Secretary of State or a delegee. If it is determined that a foreign firm engaged in sanctionable activity, State has three potential options under CISADA: (1) impose sanctions, (2) grant a waiver,²² or (3) apply the Special Rule allowing the Secretary to avoid or terminate an investigation with a pledge from the firm to cease any sanctionable activity.

In addition to enforcement actions, State officials noted that in some cases they are able to prevent investments and activity or convince firms to withdraw from Iran's energy sector, even if the activity has not yet occurred or is not sanctionable. The officials also noted that by sanctioning firms, the United States demonstrates its willingness to take that step when necessary. As sanctioned firms may still continue doing business with Iran, State officials

²¹ Pub. L. No. 104-172, § 5(c)(2)(B).

²² Pub. L. No. 104-172, §§ 4(c) and 9(c).

told us that they make every effort to reach the foreign firm before the transactions are finalized by engaging both the foreign government and foreign firm in an effort to dissuade them from the investment or activity. These officials noted that if the investment or activity has already taken place, an effort will be made to persuade the firm to end the investment or activity. They also noted that U.S. embassies play a key role in this effort by communicating to foreign firms and governments the potential consequences of continued involvement in Iran—including the imposition of sanctions.

State officials noted that in the past, firms were not sufficiently deterred from investments or activity in Iran's energy sector because no sanctions had been applied, but since State has begun imposing sanctions, these firms understand that the United States is willing to take such action, which strengthens the argument for their withdrawal. State officials told us that as a result of these efforts, dozens of firms have voluntarily stopped doing certain energy sector business with Iran, and they are seeing very few new agreements for future business. Officials also noted that several of the withdrawals have come as a result of applying the Special Rule provided for in CISADA. Since September 2010, State announced that it has obtained pledges from five foreign firms to end their business activity in Iran's energy sector, including, (1) Total of France, (2) Statoil of Norway, (3) ENI of Italy, (4) Royal Dutch Shell of the United Kingdom and the Netherlands, and (5) Inpex of Japan.²³ State officials told us that they monitor firms that have left Iran's energy sector and, so far, none of these firms have reemerged. State officials told us that despite the success of these efforts, there are foreign firms still doing business in Iran's energy sector, and as such, State plans to continue its enforcement of the ISA.

Acquisition Regulations and Procedures Updated to Implement Contractor Certification Requirement; No Indications of False Certifications or Need for Waivers

To implement the CISADA contractor certification requirement, the Civilian Agency Acquisition Council and the Defense Acquisition Regulations Council²⁴ revised the FAR by issuing an interim rule in September 2010.²⁵ The FAR now requires contracting officers to include in all solicitations a provision for the offeror to certify that the offeror, or any firm owned or controlled by the offeror, does not engage in any activities for which sanctions may be imposed under section 5 of the ISA.²⁶ In November 2010, the certification was added to the On-line Representations and Certifications Application (ORCA), the primary government repository for various contractor-submitted representations and certifications required to do business with the government. In general, prospective contractors are required to complete annual representations and certifications in ORCA and certify that they are current and accurate.²⁷ Agency contracting officers are required to either reference the date of ORCA verification in the contract file or include a paper copy of the electronically submitted representations and certifications in the file as part of the award selection process to ensure that a contractor has made this and other required certifications.

²³ We separately reported that two of the five firms, Total and Royal Dutch Shell, had no reported sales of refined petroleum products to Iran from July 2010 through December 2011 based on open sources. ([GAO-12-321R](#).)

²⁴ Revisions to the FAR are prepared and issued through these councils, which are made up of representatives from the largest federal agencies.

²⁵ The interim rule implemented the certification requirement and was subsequently finalized in November 2011, without significant changes. 75 Fed. Reg. 60254 (Sept. 29, 2010), and 76 Fed. Reg. 68027 (Nov. 2, 2011).

²⁶ FAR § 25.1103(e). The FAR provides for exemptions to the certification requirement as defined in the Trade Agreements Act of 1974 (19 U.S.C. § 2518(4)).

²⁷ FAR § 4.1201.

The acquisition councils also revised the FAR, in accordance with CISADA, to provide remedies for false certification and procedures for obtaining a waiver²⁸ of the certification requirement. If the head of an executive agency determines that a firm has submitted a false certification, the agency shall terminate the contract or suspend or debar the contractor in accordance with procedures in FAR subpart 9.4 for a period not to exceed 3 years.²⁹ According to State officials, agency contracting officers are not in a position to determine that firms are engaging in activity for which sanctions may be applied and rely on State to make that determination. As noted, all 13 firms sanctioned by State pursuant to the ISA were excluded from government contracting, or were in the process of being excluded. None of the 13 firms held any government contracts, submitted an offer, or were registered to respond to solicitations after the certification requirement went into effect. Therefore, there is no evidence of false certifications or need for waivers of the certification requirement.

The CISADA contractor certification requirement applies to prospective contractors who certify that neither they nor any firms owned or controlled by them engage in activity for which sanctions may be imposed under section 5 of the ISA. While the certification does not apply to subcontractors, the FAR specifies that contractors shall not enter into any subcontract in excess of \$30,000 with debarred contractors, other than for commercially available items.³⁰ As noted, the firms sanctioned by State pursuant to the ISA were listed in EPLS, or were in the process of being listed, making them ineligible to receive government contracts.

²⁸ 76 Fed. Reg. 68027-28; FAR § 25.703-2; and FAR § 25.703-4.

²⁹ FAR §§ 25.703-2(b), 9.406-4.

³⁰ FAR § 9.405-2(b).

Agency Comments

The Department of State provided technical comments on a draft of this report, which we incorporated as appropriate.

As agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution until seven days from the report date. At that time, we will send copies to the Secretary of State. In addition, the report will be available at no charge on the GAO website at <http://www.gao.gov>.

If you or your staff have questions about this report, please contact me at (202) 512-4841 or martinb@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report were John Neumann, Assistant Director; Grace Lui; Angela Pleasants; and Bradley Terry.

Sincerely yours,



Belva M. Martin
Director, Acquisition and Sourcing Management

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