



## OFAC Adopts New Sanctions Targeting Hizballah's Financial and Logistics Networks

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### Overview

- The HFSR apply to traditional U.S. banks and financial institutions—but importantly—the HFSR also apply to a broad array of nontraditional “financial institutions” (an expansively defined term) located in, or organized under the laws of, the United States or any jurisdiction within the United States, such as jewelry stores and car dealerships. As a result, a much wider array of businesses need to conduct restricted party screening and monitor their activities as related to FFIs.
- Because the HFSR prohibit or restrict both the opening **and maintaining** of accounts for FFIs, U.S. financial institutions need not take any positive action or process a single transaction to be exposed to potential penalties. In other words, the mere failure to timely close an account is a basis for penalty exposure—even without any act on behalf of a business to process restricted transactions subject to the HFSR. U.S. financial institutions may use a new general license to close prohibited accounts. However, use of the general license will trigger a mandatory reporting requirement, which may, in turn, expose regulated parties to further scrutiny.
- The HFSR apply to FFI activities conducted “in any location or currency.” Accordingly, FFIs must take care to ensure that their activities globally (not only those that touch the United States or the U.S. dollar) do not involve any activities prohibited under the HFSR. Designation as an entity engaging in such sanctionable activities will have far-reaching consequences in terms of the non-U.S. financial institution’s ability to operate globally.

- In addition to heightened know-your-customer (KYC) procedures, some non-U.S. financial institutions have started to require detailed explanations from existing customers on a transaction-specific basis for transactions exceeding a certain value threshold. These types of practices, as well as derisking practices involving the closing of risky customer accounts, are expected to become more prevalent in the wake of new requirements such as these.
- U.S. financial institutions that violate the HFSR may be fined USD \$250,000, or twice the transaction value, or subject to criminal penalties of \$1 million and/or 20 years of imprisonment per violation.

## **I. Application Beyond Traditional Banks**

Although the primary effect of the HFSR is to regulate U.S. banks' opening or maintaining of correspondent or payable-through accounts of FFIs, the regulatory definitions make the HFSR applicable to many nonbanking entities as well. In particular, the HFSR definition of "financial institution" is exceptionally broad and includes not only banks, exchange houses, investment companies and branches of FFIs in the United States, but also any "dealer in precious metals, stones or jewels," as well as any "business engaged in vehicle sales, including automobile, airplane and boat sales." Accordingly, U.S. entities, such as jewelry stores and car dealerships, can be subject to compliance requirements under the HFSR. Though these types of U.S. businesses are unlikely to open or maintain payable-through accounts for their customers as this term is defined in the HFSR, if a U.S. jewelry store or car dealership maintains a separate account established to receive deposits from customers, those accounts may require additional scrutiny to comply with the HFSR. OFAC also has discretion to include other businesses or agencies whose transactions may be useful in "criminal, tax or regulatory matters."

## **II. HFSR Sanctionable Activities and the New HFSR List**

The HFSR provide a basis for sanctioning FFIs for knowingly engaging in any of the following (hereinafter, "HFSR Sanctionable Activities"):

1. facilitation of "significant" transaction(s) for Hizballah
2. facilitation of "significant" transaction(s) of a person identified on OFAC's Specially Designated Nationals and Blocked Persons List (SDN List) and designated for acting on behalf of, or at the direction of, or being owned or controlled by, Hizballah (such persons will be identified by a special reference to Hizballah at the end of their SDN

List entry stating that the entity is “Subject to secondary sanctions pursuant to the Hizballah Financial Sanctions Regulations”)

3. money laundering (defined as including the movement of illicit cash or cash equivalent proceeds into, out of, or through a country or financial institution) to carry out an activity described in (1) or (2) or

4. facilitation of “significant” transaction(s) or providing “significant” financial services to carry out an activity described in (1), (2), or (3).

Facilitation of a transaction in this context is broadly interpreted to include “the provision of currency, financial instruments, securities or any other transmission of value; purchasing; selling; transporting; swapping; brokering; financing; approving; guaranteeing; the provision of other services of any kind; the provision of personnel; or the provision of software, technology or goods of any kind.”

Whether the transaction is “significant” is subject to OFAC’s discretion. OFAC will undertake a review of the totality of facts and circumstances, including a consideration of the nature of the transaction, its size, the nexus between the FFI engaging in the transactions and Hizballah or other blocked parties, and the overall impact on the Act’s objectives.

Further, the HFSR Sanctionable Activities apply to transactions conducted “in any location or currency,” meaning that a transaction need not be denominated in U.S. dollars or otherwise processed through the U.S. financial system in order to be considered sanctionable under these regulations. FFIs that the United States determines are engaging in HFSR Sanctionable Activities will be designated on a new list, the “HFSR List.” Once published, the HFSR List will be available on the Counter Terrorism Sanctions page of OFAC’s website.

### **III. Impact of Designation on the HFSR List**

OFAC may impose either (a) strict conditions or (b) a complete prohibition on “the opening or maintaining in the United States of a correspondent account or payable-through account” for FFIs designated on the HFSR List.

1. Strict Conditions. The HFSR List entry may state that a “strict condition” is applicable to the opening or maintaining of a U.S. correspondent or payable-through account.

Such strict conditions may include the following:

- a. prohibiting or restricting any provision of trade finance through the correspondent account or payable-through account of the FFI

- b. restricting the transactions that may be processed through the correspondent account or payable-through account of the FFI to certain types of transactions, such as personal remittances
  - c. placing monetary limits on, or limiting the volume of, the transactions that may be processed through the correspondent account or payable-through account of the FFI
  - d. requiring preapproval from the U.S. financial institution for all transactions processed through the correspondent account or payable-through account of the FFI or
  - e. prohibiting or restricting the processing of foreign exchange transactions through the correspondent account or payable-through account of the FFI.
2. Complete Prohibition. If the HFSR List entry for the FFI does not state a strict condition, then the FFI is subject to a complete prohibition against the opening or maintaining of a correspondent or payable-through account in the United States. The HFSR provide a new general license authorizing U.S. financial institutions to engage in transactions necessary to close the account (including transferring any remaining unblocked funds to the FFI), subject to the following conditions:
- a. the account must be closed within 10 days of the FFI's designation on the HFSR List as subject to a complete prohibition
  - b. the U.S. financial institution must file a report with OFAC within 30 days of account closure that includes "full details" on the closing of the account, including "complete information" on all transactions processed or executed through the account, and on the account outside the United States to which the remaining funds were transferred.

The terms "full details" and "complete information" are not defined, making the scope and level of detail required to comply with this reporting obligation unclear. OFAC is accepting public comment on this new reporting requirement until June 14, 2016.

#### **IV. Conclusion**

In order to ensure compliance with the terms of the HFSR, traditional and nontraditional financial institutions should remain vigilant in screening parties associated with their transactions. If an FFI is designated on the HFSR List or SDN List, removal from that list can be complicated and costly. Among other measures, removal requires that the president of the

United States receive reliable assurances from the government with primary jurisdiction over the FFI that the FFI will not engage in HFSR Sanctionable Activities in the future.

As reviewed above, some FFIs have started to require detailed explanations from existing customers on a transaction-specific basis for transactions exceeding a certain value threshold in addition to implementing heightened KYC procedures. These types of practices, as well as derisking involving the closure of high-risk customer accounts, are expected to become more prevalent in the wake of the new requirements.

## Categories

International Trade

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