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Client Alert

Global Regulatory Enforcement

Growing Trend Among States Threatens Debarment for Contractors with Iran Ties

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Guilt by association seems to be a growing trend in government contracts. Under this trend, states are starting to use their contracting authority to promote U.S. foreign policy and impose mandatory debarment for policy violators. In the latest example, companies doing business with Michigan must now be sure to stay away from business dealings with Iran, or they could find themselves debarred from state contracts for three years.

Under a law signed in the final days of 2012, starting April 1, 2013, no "Iran linked business" is eligible to bid on a contract with a Michigan public entity. An "Iran linked business" is defined as either (1) "a person engaging in investment activities in the energy sector of Iran, including a person that provides oil or liquefied natural gas tankers or products used to construct or maintain pipelines used to transport oil or liquefied natural gas for the energy sector of Iran"; or (2) "a financial institution that extends credit to another person, if that person will use the credit to engage in investment activities in the energy sector of Iran." The "energy sector of Iran" is broadly defined to include "activities to develop petroleum or natural gas resources or nuclear power in Iran." However, the discouraged "investment activity" and credit under the law is that which meets or exceeds $20 million.

The energy sector of Iran has long been a target of U.S. sanctions, and Washington has taken a multitude of approaches in an effort to cripple the Iranian energy sector. Current sanction policy not only authorizes the president to impose sanctions on U.S. persons, but also authorizes the imposition of sanctions on entities traditionally thought outside the scope of U.S. sanction policy: non-U.S. financial intuitions.

Federal approval for states and local governments to enforce their own sanction-like activity against foreign companies that invest in the energy sector of Iran is another step in Washington's approach. This approval was codified in the Comprehensive Iran Sanctions Accountability and Divestment Act of 2010 ("CISADA").

Title II of CISADA provides states and local governments with two remedies to ensure that state and local funds are not provided to companies engaged in transactions with the energy sector of Iran: the government body has the option to divest the assets of the state or local government from entities engaged with Iran. Second, the state or local government is permitted to prohibit investment of assets in persons investing in the energy sector of Iran.

In passing its legislation, Michigan has joined a multitude of other states, including California and Louisiana, that have utilized their authority under CISADA to apply state and local pressure to companies conducting business with the energy sector of Iran.

Michigan intends to enforce its new law by requiring prospective contractors to certify they are not an "Iran linked business" when submitting bids. Submitting a false certification may result in a civil penalty of the greater of $250,000, or two times the amount of the contract at issue at the time the false certification was made. The law also subjects a contractor found to have submitted a false certification from bidding on a state contract for three years, even if the contractor "unlinks" itself from Iran.

Mandatory debarment has been the subject of increasing discussion in federal circles in the past year, and states like Michigan have jumped on the bandwagon in a most unique way: by passing laws prohibiting the award of state contracts to companies doing business in U.S.-sanctioned countries. In 2012, Florida and New Jersey adopted such laws, targeting contractors with ties to Cuba and Syria in the former case, and Iran in the latter. In doing so, states are recognizing the power that the threat of suspension and debarment can have on getting contractors to perform in a certain manner.