US and EU Escalate Russia Sanctions

MONDAY, SEPTEMBER 15, 2014

Last week, the United States and European Union (EU) significantly escalated financial and trade sanctions against the Russian Federation in response to what US Treasury Secretary Jacob Lew described as Russia's "blatant efforts to destabilize Ukraine." The US and EU have designated additional Russian defense firms subject to wide-ranging asset freezes and transaction prohibitions; expanded the list of Russian financial, energy, and defense firms subject to capital market restrictions; and further controlled the provision of certain goods and services to the Russian energy sector. Although the new US and EU measures are broadly similar, important differences remain between the two regimes. We expect other jurisdictions to implement similar sanctions over the coming days.

I. New US SDN Designations

The US Department of the Treasury's Office of Foreign Assets Control (OFAC) added five new Russian defense firms to its Specially Designated Nationals and Blocked Persons (SDN) list. As a result of these designations, any property or property interests of the new SDNs that are within US jurisdiction or held by US persons must be blocked, and US persons are generally prohibited from engaging in dealings with these SDNs.

II. Expansion of Capital Market Sectoral Sanctions Identifications

OFAC has also tightened capital market restrictions for entities on its Sectoral Sanctions Identifications List (SSIL) and added firms in the Russian defense sector. First, OFAC has revised Directive 1, issued pursuant to Executive Order 13662,[1] which remains applicable to SSIL designees in the Russian financial sector. Directive 1 now prohibits transactions in new issuances of equity or debt with a maturity exceeding 30 days (instead of the previous 90-day period).[2] OFAC also listed Sberbank under Directive 1, as the EU had previously done under its equivalent measures.

Second, OFAC has designated additional energy firms subject to Directive 2, issued pursuant to Executive Order 13662. Directive 2 prohibits US persons from engaging in transactions involving new debt with a greater than 90-day maturity.[3] New designees under Directive 2 are Transneft and OJSC Gazprom Neft.

Third, OFAC has issued Directive 3 pursuant to Executive Order 13662, covering new SSILs in the defense sector. Directive 3 prohibits US persons from engaging in transactions involving new debt with a greater than 30-day maturity. The only designee thus far is the Russian defense firm Rostec.

Finally, OFAC issued General License 1a, authorizing transactions involving derivative products linked to the underlying debt/equity of the SSIL designees falling under Directives 1, 2, and 3 (General License 1a is substantially similar to the previously issued General License 1, which covered only Directives 1 and 2).[4]

III. New Sectoral Sanctions Against the Provision of Certain Goods, Services or Technology to the Russian Energy Sector

OFAC has also issued a new directive pursuant to Executive Order 13662, which is unrelated to capital markets. Directive 4 prohibits "the provision, exportation, or reexportation, directly or indirectly, of goods, services (except for financial services), or technology in support of exploration or production for deepwater, Arctic offshore, or shale projects that have the potential to produce oil in the Russian Federation, or in maritime area claimed by the Russian Federation and extending from its territory" involving any new SSIL designee under this Directive.[5] OFAC has also added five energy firms under Directive 4: Lukoil, Gazprom Neft, Gazprom OAO, Surgutneftegas, and Rosneft. Some of these firms are now cross-designated under both Directive 2 and Directive 4.

OFAC has also issued General License 2, authorizing activities that are ordinarily incident and necessary to the wind down of operations, contracts, or other agreements involving persons determined to be subject to Directive 4 by September 26, 2014, and requiring a report to OFAC within 10 business days of the completion of the wind-down activities.[6]

IV. US Export Controls

The US Department of Commerce's Bureau of Industry and Security (BIS) has also increased export controls involving several Russian defense and energy firms. First, BIS added five Russian defense firms to its "Entity List." This action imposes a license requirement for the export, reexport or foreign transfer of items subject to the Export Administration Regulations (EAR) to the designated entities, with a presumption of denial.[7]

Second, BIS added five Russian energy companies (Gazprom OAO, Gazpromneft, Lukoil, Rosneft, and Surgutneftegas) to the Entity List, which requires prior licensing for the export, reexport or foreign transfer of items subject to the EAR to those companies when the exporter, reexporter or transferor knows those items will be used directly or indirectly in exploration for, or production from, deepwater, Arctic offshore, or shale projects in Russia.[8]

V. EU Sanctions

The EU has also expanded financial and trade sanctions against Russia. First, the EU added 24 persons to its "blacklist," prohibiting any national or company of an EU Member State from making any "funds and economic resources" available to the designees, and requiring the freezing of their assets under EU Member State jurisdiction.[9] This brings the total number of persons and entities subject to EU asset freeze requirements under Ukraine-related sanctions to 142 (119 individuals and 23 entities).

Second, the EU has extended its ban on the sale, supply, transfer or export, directly or indirectly, of certain dual-use goods and technologies to nine mixed Russian defense firms.[10] The new measures also restrict the provision of technical assistance, brokering and other services, and financing and financial assistance related to those goods and technologies to the listed defense firms. These measures do not apply with respect to contracts or agreements concluded before September 12, 2014. They also do not apply to the sale, supply, transfer or export of dual-use goods and technologies intended for the aeronautics and space industry, as well as to non-military end users.

Third, the EU has imposed restrictions on the provision, directly or indirectly, of the following services necessary for deepwater oil exploration and production, arctic oil exploration and production, or shale oil projects in Russia: drilling, well testing, logging and completion services, and supply of specialized floating vessels.[11] Unlike the US energy services sanctions, the EU has grandfathered all contracts concluded prior to September 12, 2014.

Fourth, the EU has expanded its sectoral sanctions in a number of respects.[12] It has reduced the maturity date (from 90 to 30 days) of new "transferable securities and money market instruments" issued after September 12, 2014 by certain previously designated Russian financial firms (Sberbank, VTB Bank, Gazprombank, Vnesheconombank, and Rosselkhozbank),[13] with which nationals or companies of EU Member States may have almost no direct or indirect involvement. The EU regulations also utilize financial terminology that is not identical to the US terminology. The EU has also prohibited all EU nationals from involvement with such financial instruments issued by three Russian energy firms (Rosneft, Transneft, and Gazprom Neft), and three Russian defense firms (OPK Oboronprom, United Aircraft Corporation, and Uralvagonzavod). For all sectoral sanctions designees (including the five Russian banks previously sanctioned), the EU has also prohibited involvement with any new loans or credit with a maturity exceeding 30 days, with certain limited exceptions.

Fifth, the EU has expanded the existing prohibition concerning goods and technologies included in the Common Military List to prohibit the provision of insurance and reinsurance services for the sale, supply, transfer or export of those goods and technologies, and related technical assistance to Russia.

VI. Conclusion

The new US and EU sanctions represent a significant escalation of sanctions against Russia by both tightening existing restrictions and broadening the scope of targeted activities and Russian entities. Although the US and EU sanctions regimes have become increasingly harmonized, differences in specific terms and scope remain, and they both contain provisions that have not yet been fully clarified in their application. Nevertheless, last week's actions indicate that both Washington and Brussels are prepared to use similar sets of measures—a combination of expanding designations, export restrictions, and sectoral sanctions—to address concerns about Russia's involvement in unfolding events in Ukraine. These developments warrant careful monitoring by firms engaged in business in Russia to ensure that ensuing compliance risks and requirements are properly taken into account.

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[1]*See* Executive Order 13662 (March 20, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_eo3.pdf.

[2]*See* Directive 1 as Amended Under Executive Order 13662 (September 12, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/eo13662_directive1.pdf.

[3]*See* Directive 2 as Amended Under Executive Order 13662 (September 12, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/eo13662_directive2.pdf.

[4]*See* General License Number 1A (September 12, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_gl1a.pdf.

[5]*See* Directive 3 Under Executive Order 13662 (September 12, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/eo13662_directive3.pdf.

[6]*See* General License Number 2 (September 12, 2014), accessible at: http://www.treasury.gov/resource-center/sanctions/Programs/Documents/ukraine_gl2.pdf.

[7] Department of Commerce, Bureau of Industry and Security, *U.S. Commerce Department Expands Export Restrictions Aimed at Russia's Defense Sector* (September 12, 2014), accessible at: http://www.bis.doc.gov/index.php/about-bis/newsroom/press-releases/107-about-bis/newsroom/press-releases/press-release-2014/742-u-s-commerce-department-expands-export-restrictions-aimed-at-russia-s-defense-sector.

[8]*Id*.

[9]*See* Council Implementing Regulation (EU) No. 961/2014 (September 8, 2014), accessible at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.271.01.0008.01.ENG.

[10] *See* Council Regulation (EU) No. 960/2014 (September 8, 2014), accessible at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.271.01.0003.01.ENG.

[11] *Id*.

[12] *Id*.

[13] *See* Council Regulation (EU) No. 833/2014 (July 31, 2014), accessible at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.229.01.0001.01.ENG.

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