

RUSSIA: US SANCTIONS

by The Swedish Club and Reed Smith LLP
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BACKGROUND

US sanctions in relation to Russia and Ukraine comprise the following:

1. A comprehensive embargo against the Crimea region of Ukraine in response to Russia's annexation of the territory.
2. A comprehensive embargo against the Donetsk and Luhansk regions of Ukraine in response to Russia's declaration of the regions as independent from Ukraine and the following military offensive.
3. Designations in relation to a number of persons and entities in and connected to Ukraine and Russia as Specially Designated Nationals ("SDNs") as a result of their role in contributing to the crisis in Ukraine.
4. Prohibitions on US banks from certain dealings in non-ruble denominated financial instruments with, or issued by, Russian sovereigns.
5. Sectoral sanctions in relation to the financial services, energy and defense and related material sectors, in respect of which a sanctions list called the Sectoral Sanctions Identification Lists ("SSI List") has been created and updated over time.

On August 2, 2017, the US significantly expanded sanctions targeting Russia when former President Trump signed into law the Countering America's Adversaries through Sanctions Act ("CAATSA"), PL 115-44 ("the Act"). The Act is significant because it codified many of the Russia-related sanctions previously imposed through executive order, thereby requiring the President to obtain Congressional approval before easing the targeted US sanctions relating to Russia. The Act also expanded several key restrictions in the oil and gas industry, and designated as SDNs a number of Russian Oligarchs and their businesses.

In December 2019, the US imposed secondary sanctions targeting persons selling, leasing, or providing vessels engaged in certain construction activities for Nord Stream 2 or TurkStream natural gas pipeline project.

In February 2022, the US imposed new sanctions on Russia in response to "the beginning of Russian invasion into Ukraine."

LEGISLATIVE FRAMEWORK

The legal framework for the US Ukraine/Russia-related sanctions includes executive orders issued by the President, and public laws (statutes) passed by Congress, such as the Act. These authorities are then codified by the US Treasury Department, Office of Foreign Assets Control ("OFAC") in its regulations, which are published the Code of Federal Regulations ("CFR").

I. Executive Orders

- 13660—Blocking Property of Certain Persons Contributing to the Situation in Ukraine (March 6, 2014).

- 13661—Blocking Property of Additional Persons Contributing to the Situation in Ukraine (March 17, 2014).
- 13662—Blocking Property of Additional Persons Contributing to the Situation in Ukraine (March 20, 2014).
- 13685—Blocking Property of Certain Persons and Prohibiting Certain Transactions with Respect to the Crimea Region of Ukraine (December 19, 2014).
- 13883—Administration of Proliferation Sanctions and Amendment of Executive Order 12851 (August 1, 2019).
- 14024—Blocking Property With Respect to Specified Harmful Foreign Activities Of The Government Of The Russian Federation (Effective Date – April 15, 2021).
- 14039—Blocking Property With Respect to Certain Russian Energy Export Pipelines (August 20, 2021).
- 14065—Blocking Property of Certain Persons and Prohibiting Certain Transactions With Respect to Continued Russian Efforts to Undermine the Sovereignty and Territorial Integrity of Ukraine (February 21, 2022)

II. Statutes

- The Act (see above), see CAATSA.
- International Emergency Economic Powers Act (“IEEPA”), 50 USC §§1701-1706, see IEEPA.
- National Emergencies Act (NEA), 50 USC §§1601-1651, see NEA.
- Chemical and Biological Weapons Control and Warfare Elimination Act of 1991, as amended (the “CBW Act”) (22 USC § 5605(b).
- Section 7503, National Defense Authorization Act for Fiscal Year 2020 - Protecting Europe’s Energy Security Act of 2019 (“PEESA”).
- Section 1242, National Defense Authorization Act for Fiscal year 2021, Protecting Europe’s Energy Security Clarification Act (“PEESCA”).

III. Code of Federal Regulations

- The Ukraine-Related Sanctions Regulations appear at 31 CFR Part 589.
- The Weapons of Mass Destruction Proliferators Sanctions Regulations (such sanctions thereunder, the “Proliferation Sanctions”) appear at 31 CFR Part 544.

IV. Federal Register Notices

79 FR 26365-14 Issuance of regulations to implement Executive Order 13660, Executive Order 13661 and Executive Order 13662, see 79 FR 26365-14. 84 FR 44671 Issuance of regulations to implement Executive Order 13883.

86 FR 35867-21 Publication of Russian Harmful Foreign Activities Directive 1.

APPLICATION: WHO DO THE US SANCTIONS APPLY TO?

I. US Persons

Under the Ukraine-Related Sanctions Regulations, so-called “primary sanctions” apply to “US Persons”—defined as: “any United States citizen, permanent resident alien, entity organized under the laws of the United States or any jurisdiction within the United States (including foreign branches), or any person in the United States.” 31 CFR § 589.312. Primary sanctions under the Ukraine-Related Sanctions Regulations include the following:

- Crimea Embargo, prohibiting US persons from engaging in most commercial transactions with Crimea (discussed on page 4)
- Donetsk and Luhansk Embargo, prohibiting US persons from engaging in most commercial transactions with these two regions (discussed on page 4)
- Blocking Provisions, prohibiting US persons from engaging in transactions with designated parties (discussed on page 4).
- Sectoral Sanctions, prohibiting US persons from specific types of transactions with designated parties (discussed on page 5).

The Russia-Related Directive Under Executive Order of August 1, 2019 (“CBW Act Directive”) applies to US banks. The definition of “US bank” includes branches, offices and agencies of foreign financial institutions that are located in the United States and otherwise meet the definition of US bank used in this Directive.

II. Non-US Persons

Ukraine-Related Sanctions also apply to non-US persons in two respects:

- First, under the International Emergency Economic Powers Act (50 USC § 1705), non-US Persons can be penalized if they “cause a violation” of US sanctions. For example, a shipowner or Club that conducts business in the US could be penalized if it makes or receives payment in US dollars for a transaction involving a Russian SDN while concealing the involvement of the SDN in the payment instructions. Such concealment unlawfully “causes” a US bank to violate US sanctions when it processes the payment. Accordingly, it is important that non-US entities ensure their US employees, contractors, vendors, banks, and other third parties with whom they deal, do not participate in transactions from which US persons are prohibited.
- Second, so-called “secondary sanctions” are restrictions that apply to non-US persons even when there is no US nexus. In the context of Ukraine-Related Sanctions, these include:
 - Special Russian Crude Oil Projects, requiring sanctions on non-US persons who make significant investments in a certain Russian crude oil projects (discussed on page 8).
 - Energy Pipelines, authorizing sanctions against non-US persons who invest in Russian energy export pipelines. Secondary sanctions can also be imposed on non-US persons who have leased, sold or provided vessels for the construction of Nord Stream 2 or TurkStream gas pipeline projects (discussed on page 8).
 - Blocking Provisions, authorizing OFAC to block non-US persons if they engage in certain activities and/or meet certain criteria (discussed on page 4).

OVERVIEW OF US SANCTIONS AGAINST RUSSIA/CRIMEA

I. Crimea Embargo

A major element of the Russia sanctions program is an embargo on Crimea that was established in 2014. Pursuant to Executive Order 13685, the US imposed comprehensive sanctions on the Crimea region of Ukraine, which includes the land territory in that region, as well as any maritime area over which sovereignty, sovereign rights, or jurisdiction is claimed based on purported sovereignty over that land territory.

US persons are prohibited from engaging in nearly all commercial transactions with Crimea including: new investment; importation into the US of goods, services or technology from Crimea; exporting or reexporting, directly or indirectly, any goods, services or technology to Crimea; facilitating any transaction with Crimea; and donating humanitarian goods to Crimea. In addition, EO 13685 added several entities to the SDN list.

II. Donetsk and Luhansk Embargo

Upon the February 2022 Russian offensive on Ukraine, the U.S. has imposed the same type of comprehensive sanctions we saw in the Crimea context. Pursuant to Executive Order 14065, US persons are prohibited from engaging in nearly all commercial transactions in these two regions including: new investment; importation into the US of goods, services or technology from Donetsk/Luhansk; exporting or reexporting, directly or indirectly, any goods, services or technology to Donetsk/Luhansk; facilitating any transaction with Donetsk/Luhansk; and donating humanitarian goods to Donetsk/Luhansk.

While the Donetsk and Luhansk are the currently defined “Covered Regions” subject to these restrictions, Executive Order 14065 contains language pointing to that this scope could readily be extended – to “such other regions of Ukraine as may be determined by the Secretary of the Treasury.”

III. Blocking Provisions/Asset Freeze

1. What is prohibited?

Pursuant to Executive Orders 13660, 13661, 13662, 13685, 14024, 14039, and 14065 OFAC designated a number of non-US persons in and connected to Ukraine and Russia. US persons cannot engage in any transactions with SDNs, and property and interests in property of SDNs that are in the possession or control of US persons or in the US must be blocked or frozen (that is to say may not be transferred, paid, exported, withdrawn or otherwise dealt in) and reported to OFAC.

The President has the power, acting through OFAC, to block and freeze the assets of non-US Persons meeting the following criteria:

- Cybersecurity: Individuals who knowingly undermine cybersecurity against a person, democratic institution, or government (such as hacking) on behalf of the Russian Government.
- Human Rights Abuses: Individuals who are responsible for commissioning serious human rights abuses in any territory “forcibly occupied” or controlled by the Russian Government.
- Abuses in Ukraine: Parties responsible or complicit in undermining democratic processes, threatening the peace, misappropriating state assets, and other abuses of power in Ukraine.
- Arms: Parties operating in the arms or related material sector in the Russian Federation.
- Crimea: Parties who “operate in the Crimea region of Ukraine” or are “a leader of an entity operating in the Crimea region of Ukraine.”

- **Donetsk and Luhansk:** Parties who “operate in” Donetsk or Luhansk, or are leaders of an entity operating in Donetsk or Luhansk.
- **Russian Industries:** Parties who operate in sectors of the Russian Federation economy as may be determined by the Secretary of the Treasury, in consultation with the Secretary of State, such as financial services, energy, metals and mining, engineering, and defense and related materiel.
- **Russian Harmful Foreign Activities:** Parties who operate in the technology or defense sector of the Russian economy, and any other sector of the Russian Economy, as determined by the Secretary of Treasury. Executive Order 14024 also authorizes sanctions on persons determined to have engaged in or attempted to engage in, but not limited to, the following activities: inflicting bodily harm or causing the death of a US citizen, person, or national of a US ally; organizing transactions for the purpose of evading US sanctions (including through the use of digital assets or currencies); and transnational corruption.
- **Energy or Gas Supplies:** Parties determined to be responsible for, complicit in, or engaged in or having attempted to interfere with or cut gas supplies or energy to the Caucasus, Asia, or Europe.
- **Governments of other Countries:** Parties who have “materially assisted” a government subject to blocking sanctions. This includes the governments of Iran, Cuba, North Korea, Syria, and Venezuela.

In addition to the blocking criteria listed above, OFAC is authorized to block and designate a non-US person when it has been determined that the person:

- Has materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services for any person blocked pursuant to an executive order.
- Has knowingly “facilitate[d] a significant transaction . . . , including deceptive or structured transactions, for on behalf of . . . any person subject to the sanctions imposed by the United States with respect to the Russian Federation.” This includes entities owned 50 percent or more, individually or collectively, by an SDN. See Section 226 of CAATSA.
 - OFAC has explained that “facilitating” a transaction refers to the provision of “assistance for a transaction from which the person in question derives a particular benefit of any kind” See FAQ 545.
 - OFAC will consider a totality of circumstances when determining whether a specific transaction is “significant”, while also providing seven factors to be considered when making that analysis. Those factors include (1) the size, number, and frequency of the transaction(s); (2) the nature of the transaction(s); (3) the level of awareness of management and whether the transaction(s) are part of a pattern of conduct; (4) the nexus between the transaction(s) and a blocked person; (5) the impact of the transaction(s) on statutory objectives; (6) whether the transaction(s) involve deceptive practices; and (7) such other factors that the Secretary of the Treasury deems relevant on a case-by-case basis. See FAQ 545. A transaction is not “significant,” however, if a US person would not require a specific license from OFAC to engage in the activity.

OFAC is required to impose secondary sanctions on non-US financial institutions that have knowingly facilitated “significant financial transactions” for any Russian person who has been designated pursuant to Ukraine-related authorities. See CAATSA 226.

2. What penalties can be imposed on non-US persons?

Non-US persons who engage in transactions with SDNs that OFAC finds to be “significant” and thus sanctionable under Section 231 of CAATSA, may face five or more of the sanctions described in Section 235 of CAATSA. These secondary sanctions include: prohibitions on Export-Import Bank assistance, export licenses for exports to sanctioned persons, prohibitions on loans to sanctioned persons of more than \$10 million over a 12-month period from any US financial institution, prohibition of any transactions in foreign exchange by the sanctioned person within the jurisdiction of the United States, and asset blocking, as well as various additional sanctions directed at financial institutions and transactions and measures against corporate executives. These measures are designed to use economic leverage to dissuade non-US persons from engaging in transactions with anyone subject to secondary sanctions.

3. How is the shipping industry affected by the blocking provisions/asset freeze?

If a shipping industry participant is blocked, US persons would be prohibited from engaging in any transactions or dealings with that SDN. The US persons would also be required to block or freeze all property and interests in property of the SDN in their possession. Non-US persons should also avoid dealings with SDNs, because the provision of goods, services and other forms of material assistance to an SDN may expose non-US persons to blocking sanctions.

4. How can I find out which parties are designated?

The full SDN List may be found at the OFAC website at SDN Human Readable Lists. It is also possible to search the list, using the OFAC search engine at Sanctions List Search Tool.

Most recently, on February 22, 2022, the U.S. designated State Corporation Bank for Development and Foreign Economic Affairs Vnesheconombank (VEB) and Promsvyazbank Public Joint Stock Company (PSB). These institutions are now blocked, along with any entities they own by at least 50%. The OFAC designation notice lists 25 blocked subsidiaries for VEB, and 17 subsidiaries for PSB – one of which is PSB Lizing OOO. As part of the designation of PSB, OFAC also sanctioned five vessels that are owned by PSB Lizing OOO:

1. **Baltic Leader** (IMO: 9220639), a Russian-flagged roll-on roll-off cargo vessel with a gross registered tonnage of 8831;
2. **Linda** (IMO: 9256858), a Russian-flagged crude oil tanker with a gross registered tonnage of 61991;
3. **Pegas** (IMO: 9256860), a Russian-flagged crude oil tanker with a gross registered tonnage of 61991;
4. **Fesco Magadan** (IMO: 9287699), a Russian-flagged container ship with a gross registered tonnage of 7519; and
5. **Fesco Moneron** (IMO: 9277412), a Russian-flagged container ship with a gross registered tonnage of 7519

Denis Aleksandrovich Bortnikov (Deputy President of VTB Bank), Petr Mikhailovich Fradkov (General Director of JSC Russian Export Center, a VEB subsidiary), and Vladimir Sergeevich Kiriyyenko (CEO of VK Group, the parent company of Russia’s top social media platform) have also been sanctioned in OFAC’s latest February 2022 action.

IV. Sectoral Sanctions: The Directives

Since 2014, the OFAC has maintained four “Directives” that impose targeted sanctions upon key elements of the Russian economy, all of which were promulgated under Executive Order 13662. The primary purpose of Executive Order 13662 was to focus on entities in certain sectors of the Russian economy, such as “financial services, energy, metals and mining, engineering, and defense and related materiel.”

Each Directive governs activities between US persons and those listed on the Sectoral Sanctions Identifications SSI List. The SSI List is organized according to the four Directives. The SSI List may be searched on the OFAC website at Sectoral Sanctions Identifications (SSI) List.

Unlike the SDN List, which includes blocked persons and prohibits virtually all activity with so-called SDNs, the SSI List designations result in narrow prohibitions that are limited to those activities in the identified sectors targeted by the Directives. Note that, with all the Directives, sanctions that apply to entities on the SSI List also apply to any entities that are owned 50 percent or more by one or more persons on the SSI List, see 50% Rule. Therefore, providing funds to a non-listed entity that is owned (50% or more) by a listed entity is considered a prohibited provision of funds to the listed entity.

1. Directive 1 (as amended on September 29, 2017) Under Executive Order 13662 (13-Day New Debt/No Equity) targeting Russia's financial services sector

Directive 1 was established in 2014 to target the financial services sector of the Russian economy. This directive originally prohibited US persons (or those within the United States) from engaging in transactions in, providing financing for, or otherwise dealing in new debt with a maturity of longer than 90 days (July 16, 2014 version) and then 30 days (September 12, 2014 version), or equity for persons identified on the SSI List under Directive 1.

However, under the Act, OFAC was required to modify Directive 1 to reduce the "new" debt prohibition to 14 days. This was done on September 29, 2017, and the reduction came into effect in respect of new debt or new equity issued on or after November 28, 2017.

2. Directive 2 (as amended on September 29, 2017) Under Executive Order 13662 (60-Day New Debt) targeting Russia's energy sector

Directive 2 targets Russia's energy sector of the Russian economy by prohibiting transactions in, the provision of financing for, and other dealings in new debt with a maturity of longer than 60 days for persons identified on the SSI List under Directive 2. Originally, Directive 2 covered new debt with a maturity of longer than 90 days but the Act required OFAC to reduce the period to 60 days. This was done on 29 September 2017, and the reduction came into effect in respect of new debt issued on or after November 28, 2017.

3. Directive 3 (30-Day Debt) Under Executive Order 13362 targeting Russia's defense and related material sector

Directive 3 targets the Russian defense and related material sector by prohibiting all transactions in, the provision of financing for, and other dealings in new debt of longer than 30 days for persons identified on the SSI List under Directive 3.

4. Directive 4 (as amended on October 31, 2017) under Executive Order 13662 (Energy Industry Prohibitions) further targeting Russia's energy sector

Directive 4 expands on the sanctions targeting the Russian energy sector. The original version of Directive 4 prohibited US persons from: (1) "the provision, exportation, or reexportation, directly or indirectly, of goods, services (except for financial services), or technology"; (2) "in support of exploration or production for deepwater [underwater activities at depths of more than 500 feet], Arctic offshore, or shale projects" (hereafter "Covered Projects"); (3) "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"; (4) that involve any person identified on the SSI List under Directive 4, including that person's property, or its interests in property.

OFAC modified Directive 4 to prohibit US persons not only from providing goods, services and technology for Covered Projects in Russia, but also to such projects anywhere in the world, if they involved persons designated under Directive 4. Notably, the expansion of Directive 4 to reach Covered Projects beyond Russia applied only to “new” Covered Projects where the Directive 4 target “has a controlling interest or a substantial non-controlling ownership interest in such a project defined as not less than a 33 percent interest.” The amendment was made on October 31, 2017 and covers projects that were initiated on or after January 29, 2018.

6. Directive 1A under Executive Order 14024 (Russia-related Sovereign Debt Directive)

On February 22, 2022, OFAC issued Russia-related Directive 1A under E.O. 14024, “Prohibitions Related to Certain Sovereign Debt of the Russian Federation” (the “Russia-related Sovereign Debt Directive”), amending and superseding Directive 1 under E.O. 14024. This extends existing sovereign debt prohibitions to cover participation in the secondary market for bonds issued after March 1, 2022 by the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, or the Ministry of Finance of the Russian Federation.

V. Proliferation Sanctions

Following a March 2018 chemical attack by individuals allegedly associated with Russian government forces in Salisbury, England, the US implemented several punitive measures against Russia. The sanctions prohibit US banks from: (1) participating in the primary market for non-ruble denominated bonds issued by a Russian sovereign and (2) lending non-ruble denominated funds to the Russian sovereign. OFAC imposed these sanctions through the CBW Act Directive of August 1, 2019, which was issued pursuant to Executive Order 13883 (Administration of Proliferation Sanctions and Amendment of Executive Order 12851), 31 CFR § 544.802, and section 307(b) of the CBW Act.

A “Russian sovereign” for purposes of the CBW Act Directive means “any ministry, agency, or sovereign fund of the Russian Federation, including the Central Bank of Russia, the National Wealth Fund, and the Ministry of Finance of the Russian Federation,” but does not include state-owned enterprises. The CBW Act Directive does not prohibit US banks from participating in the secondary market for Russian sovereign debt.

VI. Special Russian Crude Oil Projects

The President is required, unless he/she determines it is not in US national security interests, to impose sanctions on any person who “knowingly makes a significant investment” in a “special Russian crude oil project,” defined as “a project intended to extract crude oil from (i) the exclusive economic zone of the Russian Federation in waters more than 500 feet deep; (ii) Russian Arctic offshore locations; or (iii) shale formations located in the Russian Federation.”

VII. Energy Pipeline Secondary Sanctions

The US has also imposed secondary sanctions targeting non-US persons engaged in certain transactions related to Russian energy pipelines.

Investments

The Act gives the President the power to impose (but does not require) secondary sanctions on non-US persons who knowingly: (1) make an investment of USD 1 million or more (or USD 5 million or more over a 12-month period) that directly and significantly contributes to enhancing Russia’s ability to construct energy export pipelines or (ii) sell, lease, or provide to the Russian Federation, goods, services, technology, information, or support (valued at USD 1 million or more, or during a 12-month period with an aggregate value of USD 5 million or more) that could directly and significantly facilitate the maintenance or expansion of the construction, modernization, or repair of energy pipeline.

Pipe-laying Vessels

PEESA, which was signed into law in December 2019, requires the President to impose secondary sanctions on non-US persons who knowingly: (1) sell, lease or provide vessels engaged in pipe-laying at depths of 100 feet or more below sea level for the construction of the Nord Stream 2 pipeline project or the TurkStream pipeline project (a pipeline that runs from Russia to Turkey across the Black Sea) and any successor to either project; or (2) facilitate deceptive or structured transactions to provide those vessels for the construction of such a project.

The secondary sanctions consist of: (1) blocking sanctions and prohibitions on all transactions in US property and interests in property of any person sanctioned under PEESA if such property and interests in property are in the US or in the possession or control of a US person; and (2) prohibiting the entry into the US and the issuance of a US visa to any non-US person that is a corporate officer or principal shareholder of a person sanctioned under PEESA.

In January 2021, the United States congress enacted PEESCA, which threatens sanctions on companies providing, among other things, insurance, underwriting, inspection, pipe-laying, services related to retrofitting, upgrading, or tethering pipe-laying vessels, or pipe-laying vessels, goods, services, information, technology, or other support for either project.

EXPORT CONTROLS

I. Commercial and Dual-Use Export Controls

In coordination with the sanctions programs administered by OFAC, the US Department of Commerce, Bureau of Industry and Security (“BIS”) administers export controls that impact trade with Russia. On August 6, 2014, BIS amended the Export Administration Regulations (“EAR”) to include the “Russian Industry Sector Sanctions” at section 746.5. These restrictions impose a license requirement for the export to Russia of certain items if the exporter, reexporter, or transferor knows that the item “will be used directly or indirectly in exploration for, or production of, oil or gas in Russian deepwater (greater than 500 feet) or Arctic offshore locations or shale formations in Russia, or are unable to determine whether the item will be used in such projects.” The items subject to this license requirement include items classified under the following Commerce Control List Export Control Classification Numbers (ECCNs): 0A998, 1C992, 3A229, 3A231, 3A232, 6A991, 8A992, 8D999, as well as EAR99 items identified in Supplement No. 2 to Part 746. BIS also established a policy of denial for such license applications. BIS further imposed a license requirement (subject to a policy of denial) for all exports, reexports, or transfers to Russia of items subject to the EAR if intended, in whole or in part, for a military end- use or military end-user in Russia.

II. Military/Defense Export Controls (ITAR)

On March 27, 2014, DDTC placed a hold on the issuance of International Traffic in Arms Regulations (“ITAR”) licenses for the export of defense articles and defense services to Russia. On April 28, 2014, DDTC changed its hold on licenses to a policy of denial for defense articles or defense services to Russia or occupied Crimea. DDTC also began revoking existing licenses for defense articles and services. DDTC currently reviews defense article export licenses on a case-by-case basis to determine the export’s contribution to Russia’s military.

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