

E-ALERT | International Trade Controls

July 17, 2014

U.S. TREASURY DEPARTMENT IMPLEMENTS NEW SANCTIONS TARGETING RUSSIAN FINANCIAL AND ENERGY SECTORS; NAMES NEW BLOCKED PARTIES

EU IMPOSES ADDITIONAL SANCTIONS RELATED TO UKRAINE CRISIS

On July 16, 2014, the U.S. Treasury Department's Office of Foreign Assets Control ("OFAC") imposed an additional wave of sanctions against Russian entities in the financial, energy, and defense sectors. OFAC established a [new Sectoral Sanctions Identifications List](#) (the "SSI List"), which identifies two Russian financial institutions and two Russian energy companies for targeted sanctions. Simultaneously, OFAC announced the addition of five individuals and 11 entities to the [List of Specially Designated Nationals and Blocked Persons](#) (the "SDN List"). The U.S. Department of Commerce's Bureau of Industry and Security ("BIS") added the same 11 entities to its Entity List.

The highly anticipated sectoral sanctions target Russian banks Gazprombank OAO and Bank for Development and Foreign Economic Affairs State Corporation (otherwise known as "VEB"), and Russian energy firms Rosneft Oil Company and OAO Novatek. These four parties are not subject to comprehensive blocking measures; rather, the new sanctions prohibit U.S. persons and persons in the United States from dealing in certain new debt of these parties and, in the case of the two banks, new equity. These targeted sanctions were authorized by the Secretary of the Treasury under [Executive Order 13662](#), which was signed by the President in March.

The new additions to the SDN List include eight Russian arms firms, three parties asserting unauthorized governmental control over parts of Ukraine, one entity allegedly involved in the misappropriation of Ukrainian state assets, and four Russian government officials.

In addition, the European Council has taken action to expand the EU sanctions relating to the Ukraine crisis, adding 11 additional individuals to the sanctions list, and agreeing to take additional measures in the near term to further expand the EU sanctions list and to impose certain investment-related sanctions targeting Russia and Crimea.

I. U.S. SANCTIONS

Sectoral Sanctions Against Russian Entities in the Financial Services and Energy Sectors

The new SSI List and its associated provisions implement new directives, pursuant to Executive Order 13662, targeting designated firms in the financial services and energy sectors in Russia. These SSI directives prohibit U.S. persons from engaging in transactions, financing, or other dealings related to new debt of longer than 90 days maturity with listed persons, their property, or their property interests. The financial services directive also prohibits transactions, financing, and dealings related to new equity involving named parties, their property, or their property interests. As with other OFAC sanctions programs, "U.S. persons" include companies formed under U.S. law,

wherever located; U.S. citizens and permanent residents, wherever located or employed; and any person or entity within the United States.

- Directive 1 applies to financial services entities Gazprombank OAO and VEB. Gazprombank OAO is a Russian financial services institution that serves companies involved in Russia's energy industry, as well as other sectors. VEB is a Russian state-owned financial services institution that serves as the Russian government's development bank and payment agent, including for its sovereign debt. Directive 1 prohibits U.S. persons from transacting in, financing, or dealing in both new debt with greater than 90 days maturity, and new equity.
- Directive 2 targets energy firms Rosneft, the world's largest oil and gas company, and OAO Novatek, Russia's largest independent natural gas producer. Directive 2 prohibits U.S. persons from transacting in, financing, or dealing in new debt with greater than 90 days maturity, but does not prohibit transactions or financing for new equity.

OFAC has clarified that the new directives apply to transactions, financing, and other dealings that involve entities in which one of the four named parties on the SSI List has an ownership interest of 50% or more, consistent with earlier sanctions guidance.

According to OFAC guidance on the new measures, "debt" includes bonds, loans, credit extensions, loan guarantees, letters of credit, drafts, bankers acceptances, discount notes or bills, and commercial paper. "Equity" includes stocks, share issuances, depositary receipts, and "any other evidence of title or ownership." The provisions apply to the debt or equity issued or created on or after July 16, 2014 – they do not apply to transactions that have previously concluded, or to transactions involving equity or debt that were issued or created prior to July 16, 2014. The prohibitions do apply to the rollover of existing debt, however, if the rollover generates or results in new debt exceeding 90 days in maturity. Finally, OFAC also issued General License No. 1 on July 16, 2014, authorizing transactions and dealing in derivative products whose value is linked to new debt or new equity that would be within the scope of the new SSI directives.

U.S. persons are required to reject prohibited transactions or dealings in new debt or new equity under these sanctions, and U.S. financial institutions will likely be required to report their rejection to OFAC. OFAC guidance reflects that under Section 501.604 of the Reporting, Procedures and Penalties Regulations (31 C.F.R Part 501), U.S. financial institutions are required to report their rejection to OFAC within 10 business days.

As a result of the sectoral sanctions, the named banks and energy companies will not be able to receive medium- and long-term loans in U.S. dollars or from U.S. persons, and the financial institutions' ability to issue new equity to or involving U.S. persons and persons in the United States will be impaired. However, OFAC's guidance on the SSI directives provides that U.S. banks may continue to process U.S. dollar-clearing transactions for or involving the named parties as long as those activities do not involve transacting or otherwise dealing in prohibited transaction types.

Companies should take steps to ensure that transactions are appropriately screened against the new SSI List, in addition to existing screening against the SDN List, Entity List, and other restricted-party lists, to identify potentially prohibited transactions involving new debt or new equity. But it should be understood that the directives do not constitute a blocking action, and entities named on the SSI List will not automatically be added to the SDN List, which prohibits all unauthorized transactions with designated parties and requires U.S. persons to block the property or property interest of named entities. Consequently, U.S. firms may continue to conduct business with Rosneft and other entities subject to the sectoral sanctions, though they will need to be mindful of not engaging in activities prohibited by the sectoral sanctions, such as extending commercial financing terms of more than 90 days or making new equity investments in the two named banks.

Transactions not specifically prohibited by the SSI List provisions are permissible, provided that they do not violate the provisions of Executive Orders 13660, 13661, or 13662 (which were the subject of our prior e-alerts on [March 6, 2014](#), [March 18, 2014](#), and [March 21, 2014](#)) or OFAC's Ukraine-Related Sanctions Regulations (31 C.F.R. Part 589). In that regard, it is noteworthy with respect to Rosneft that OFAC has designated Rosneft's president and chairman of the board, Igor Sechin, as an SDN pursuant to Executive Order 13661.

Additions to the OFAC SDN List and BIS Entity List

On July 16, 2014, the Treasury Department also designated and blocked the assets of eight defense technology firms under Executive Order 13661 for operating in Russia's arms and related materials sector; two entities and one individual under Executive Order 13660 for threatening the peace, stability, sovereignty or territorial integrity of Ukraine; an oil shipping facility in the Crimean Peninsula, sanctioned under Executive Order 13660, that is allegedly complicit in the misappropriation of Ukrainian assets; and four Russian government officials pursuant to Executive Order 13661.

Notable blocked defense parties include Kalashnikov Concern, Russia's largest firearms firm whose products include various assault rifles, grenades, and other military weapons. Kalashnikov Concern is a subsidiary of the State Corporation of Russian Technologies ("Rostec"). Additionally, both the Luhansk People's Republic ("LPR") and the Donetsk People's Republic were designated on the SDN List for asserting government control over a portion of Ukraine without the Ukrainian government's authorization. The self-declared "prime minister" of the Donetsk People's Republic, Aleksandr Borodai, is also a newly designated party.

The property and property interests of designated parties in the United States or that are in the possession or control of a U.S. person are blocked. They cannot be transferred, paid, exchanged or otherwise dealt with by U.S. persons absent a license or other form of OFAC authorization. Pursuant to long-standing OFAC guidance, the property or property interest of entities owned 50% or more by an SDN are also blocked, and U.S. persons may not engage in transactions involving entities in which a designated person owns a 50% or greater interest.

According to OFAC, Kalashnikov Concern transactions that occurred prior to July 16, 2014 are not impacted by the recent amendment to the SDN List, provided that Kalashnikov Concern does not have any remaining interest in the transaction. U.S. parties benefitting from such a transaction may lawfully retain or sell their Kalashnikov products. However, OFAC advises U.S. persons or entities that are involved in pending transactions with Kalashnikov Concern or in which Kalashnikov Concern has an interest to consult the agency for further instruction before selling the product or taking further action, regardless of whether they are in possession of the product.

In addition to these SDN designations by OFAC, BIS added the same 11 entities (but not the new SDN individuals) to its Entity List under the Export Administration Regulations ("EAR," 15 C.F.R. Parts 730-774). The effect of the Entity List designation is to prohibit export, reexport or transfer within Russia or any other country of any item "subject to the EAR" to or for any of these 11 entities. As a result, BIS licensing would be required for any person – including non-U.S. persons – to export, reexport, transfer or supply any U.S.-origin items, or any item with more than 25% U.S.-origin content, with knowledge or reason to know it was intended for one of these parties added to the Entity List, with a presumption of denial for such a license.

II. EU SANCTIONS

On July 11, 2014, the EU Council designated 11 additional Ukrainian individuals involved in the separatist movements in Eastern Ukraine for asset freezing measures. EU parties (i) must freeze all funds and “economic resources” belonging to, owned, held, or controlled by the newly designated parties, and (ii) are prohibited from making available funds or “economic resources,” directly or indirectly, to or for the benefit of the designated parties. (“Economic resources” include “assets of every kind, whether tangible or intangible, movable or immovable, which are not funds, but which may be used to obtain funds, goods or services.”) Dealings with entities that are owned or controlled by the designated parties are also prohibited.

On July 16, 2014, the EU Council agreed to [expand the legal basis for the EU sanctions](#), with a view of targeting entities supporting the destabilization of Ukraine. The EU will decide by the end of July on the names of the additional sanctioned parties. Separately, the EU Council decided to (i) suspend new financing operations in Russia by the European Investment Bank in Russia, (ii) coordinate with the EU Member States for the suspension of new European Bank for Reconstruction and Development financing in Russia, and (iii) re-assess EU-Russia cooperation programs with a view of their potential suspension. The EU Council has also indicated that it may issue further restrictions on investments in Crimea. Those measures will be further detailed in a Council Decision and/or Regulation, expected to be published later this month.

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We are following the above-mentioned sanctions developments closely and will provide further updates as they evolve. We are particularly well-positioned to advise companies and individuals on compliance with the U.S. and EU sanctions related to the Ukraine crisis, as well as on the broader impact of the crisis on foreign investment in both Ukraine and Russia and other legal and commercial interests in the region.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our international trade controls practice group:

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