

CLIENT ALERT

# Administration Issues Broad Guidance to Implement New Russia Sanctions Contained in the Countering America's Adversaries Through Sanctions Act

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The U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") and the U.S. Department of State have issued a series of regulatory amendments and guidance to implement new sanctions for Russia in the Countering America's Adversaries Through Sanctions Act ("CAATSA"), which became law on August 2, 2017. The provisions in CAATSA tighten the prohibitions for U.S. persons for certain activity in and outside of Russia, particularly activity related to Russia's financial and energy sectors, and authorize broad new secondary sanctions for non-U.S. persons for certain activity related to Russia and sanctioned persons. The revised Directives, issued pursuant to Executive Order ("E.O.") 13662, provide greater clarity on the prohibitions on U.S. persons, and the guidance on secondary sanctions further defines the scope of activities that could result in sanctions on non-U.S. persons engaged in the activities identified in CAATSA. This alert outlines the amendments and guidance for some of the key provisions of the statute.<sup>1</sup>

### I. Changes to Primary Sanctions Provided for in the Ukraine-/Russia-Related Directives

On September 29, 2017, OFAC issued revised Directives 1 and 2 of the Ukraine/Russia-related sectoral sanctions, originally issued pursuant to E.O. 13662, to shorten the permissible length of maturity for the debt of listed entities dealt in

<sup>1</sup> The modified Directives 1, 2, and 4 and additional guidance by OFAC, including updated Frequently Asked Questions, are available [here](#). For additional information on CAATSA, see Willkie's client memorandum, "President Trump Signs Omnibus Sanctions Bill into Law, Tightening Sanctions Against Russia, but Leaving Open Questions on Implementation," available [here](#).

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by U.S. persons. OFAC made these amendments in accordance with Section 223(b) of CAATSA, and the changes to Directives 1 and 2 will come into effect on November 28, 2017.

Specifically, the modified Directive 1 prohibits all transactions in, provision of financing for, and other dealings by a U.S. person or within the United States in new debt of longer than 14 days maturity or new equity by, on behalf of, or for the benefit of persons operating in Russia's financial sector, determined to be subject to the Directive. The modified restriction applies only for new debt issued on or after November 28, 2017. The previous limitations of 90 days for new equity or debt issued on or after July 16, 2014 or 30 days for new equity or debt issued on or after September 12, 2014 remain in place.

Similarly, the modified Directive 2 prohibits all transactions in, provision of financing for, and other dealings by a U.S. person or within the United States in new debt of longer than 60 days maturity by, on behalf of, or for the benefit of persons operating in Russia's energy sector, determined to be subject to this Directive. This modified restriction applies only for new debt issued on or after November 28, 2017. The prohibitions on transactions or dealings in new debt of greater than 90 days maturity remain in place for the previous periods.

OFAC also revised Directive 4, effective January 29, 2018, expanding its application to certain new projects including projects outside of Russia. The revisions to Directive 4 expand on the previous restrictions to include a prohibition on the provision, exportation, or re-exportation, directly or indirectly, by U.S. persons of goods, services (except for financial services), or technology in support of exploration or production for new deepwater, Arctic offshore, or shale projects, initiated on or after January 20, 2018, that have the potential to produce oil in any location and that involve any person determined to be subject to the directive that has not less than a 33 percent interest or ownership of a majority of the voting interests.

The revised directive provides greater clarity as to the scope of the revisions required by CAATSA, which required OFAC to modify the directive to prohibit the provision of goods or services to "new" covered projects in which a person subject to the directive has a 33 percent interest or "controlling interest." The revised directive makes clear that "new" projects refers to projects "initiated" on or after January 20, 2018, and that a "controlling interest" requires an objective threshold that the listed person owns a majority of the voting interests.

### **II. New Secondary Sanctions Authorized by CAATSA**

#### **A. Transactions for Russian Persons Subject to U.S. Sanctions**

Section 228 of CAATSA amends the Support for the Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014 to include the mandatory imposition of sanctions against persons that the president determines have knowingly facilitated a "significant transaction" for or on behalf of "any person subject to sanctions imposed by the United States with respect to the Russian Federation." OFAC guidance clarifies that "any person subject to sanctions imposed

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by the United States" includes persons listed on OFAC's List of Specially Designated Nationals and Blocked Persons List ("SDN List") and the Sectoral Sanctions Identification List ("SSI List"), and any persons subject to sanctions by way of the 50 percent rule, meaning any entity owned 50 percent or more by persons on the SDN or SSI List.

However, the OFAC guidance also provides several circumstances under which a transaction would not be considered significant, including any transaction that would otherwise not require a U.S. person to obtain a license from OFAC. Additionally, a transaction with a person "subject to U.S. sanctions" based solely on inclusion on the SSI List would not be considered significant unless the transaction also involved deceptive practices, including attempts to conceal the parties or evade sanctions.

The OFAC guidance further states that OFAC will consider the totality of the facts and circumstances of a transaction on a case-by-case basis to determine whether a transaction is "significant" for the purpose of this Section 228. The guidance also lists seven broad factors that will be taken into consideration when evaluating the transaction: (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.

The above factors define the application of Section 228 to avoid some of the more drastic implications for non-U.S. firms involved in any business with persons subject to the sectoral sanctions.

### **B. Transactions by Foreign Financial Institutions for SDNs**

Section 226 of CAATSA amends Section 5 of the Ukraine Freedom and Support Act ("UFSA") and requires the president to sanction foreign financial institutions that the president determines have knowingly engaged in significant transactions involving certain defense- and energy-related activities or for knowingly facilitating significant transactions on behalf of any Russian person listed on the SDN List designated pursuant to UFSA or any of the Ukraine-/Russia-related Executive Orders. Under the prior version of the UFSA, these sanctions were discretionary. OFAC guidance advises that a foreign financial institution will not be sanctioned under Section 226 for facilitating transactions on behalf of persons listed on the SSI List. The guidance also provides that OFAC will consider the totality of the circumstances in determining whether a transaction is "significant" and will apply the same seven broad factors listed above.

### **C. Transactions Involving the Defense and Intelligence Sectors**

Section 231 requires that the president, beginning January 29, 2018, impose sanctions on persons who the president determines to have knowingly engaged in a significant transaction with a person involved in the intelligence or defense sectors of the Russian government. On October 27, 2017, the U.S. Department of State published a list of persons determined to be "part of, or operating for or on behalf of, the defense or intelligence sectors of the Government of the

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Russian Federation.” The State Department guidance states that the Department will evaluate transactions on a case-by-case basis to determine whether the transaction is “significant,” and includes three factors of particular importance: (1) the significance of the transaction to U.S. national security and foreign policy interests; (2) the nature and magnitude of the transaction; and (3) the relation and significance of the transaction to the defense or intelligence sector of the Russian government.

The State Department guidance advises that the Department's focus is expected to be on significant transactions of a defense or intelligence nature with the listed entities. For transactions for goods or services with purely civilian end-uses and/or civilian end-users, and not involving entities in the intelligence sector, these factors will generally weigh heavily against a determination that such a transaction is significant. Furthermore, for transactions that are necessary pursuant to Russia's Federal Security Service regulations regarding the importation of information technology products to Russia and the payment of fees related to licenses or other similar requirements administered by the Federal Security Service, these factors also will weigh heavily against a determination that the transaction is significant.

### **D. Transactions Involving the Energy Sector**

Sections 225 and 232 of CAATSA authorize secondary sanctions related to Russia's energy sector. Section 225 amends section 4(b) of the UFGA and requires the president to sanction any foreign person who knowingly makes a significant investment in a “special Russian crude oil project” on or after September 1, 2017, defined as any project in the exclusive economic zone of Russia in waters more than 500 feet deep, Russian Arctic offshore, or shale projects. The State Department guidance states that, among a number of other factors, whether a transaction is “significant” may be determined by the significance of the transaction to U.S. national security and foreign policy interests, as well as its significance to the Russian energy sector. The nature and magnitude of the investment, including the size of the transaction relative to the project's overall capitalization, will also be weighed.

In addition, Section 232 authorizes the president to impose sanctions on persons the president determines to have knowingly made, on or after August 2, 2017, a significant investment that has a fair market value of \$1,000,000 or more, or a series of investments that have an aggregate fair market value of \$5,000,000 or more over 12 months, and that (1) directly and significantly contributes to Russia's ability to construct energy export pipeline projects initiated on or before August 2, 2017, or that (2) provides significant goods, services, technology, information or support to “directly and significantly facilitate the maintenance or expansion of the construction, modernization, or repair of such energy export pipelines.” The State Department guidance specifies that Section 232 implementation will be focused on “energy export pipelines (1) that originate in the Russian Federation; and (2) transport hydrocarbons across an international land or maritime border for delivery to another country.” The guidance also states that a project is considered to have been initiated when a contract for the project is signed. For example, investments and loan agreements made prior to August 2, 2017 would not be subject to Section 232 sanctions, nor would investments or other activities related to the standard

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repair and maintenance of pipelines in existence on, and capable of transporting commercial quantities of hydrocarbons, as of August 2, 2017.

### III. Conclusion

Due to these recent changes, companies should ensure that their policies and procedures for activity involving Russia are updated and account for these new sanctions. U.S. companies should pay close attention to any credit or payment terms with entities subject to Directive 1 or 2, as well as Directive 3, and ensure that these terms reflect the revised prohibitions, as well as the provision of services to non-conventional oil projects involving listed Russian entities. Both U.S. and non-U.S. companies should also be aware of the provisions of CAATSA that require or authorize the president to impose sanctions for certain sector-specific activity in Russia, including transactions involving listed persons.

If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

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