

Ukraine Crisis Update: US and EU Expand and Align Sanctions

The US and EU take coordinated action to broaden and align their Russia-related sanctions — which may evolve further depending on Ukraine peace plan progress.

On September 12, 2014, the US and the EU announced new and expanded sanctions on certain entities and projects in Russia. These measures reflect growing coordination between the US and the EU to impose tougher and more consistent sanctions that target certain sectors of the Russian economy, in an effort to pressure the Russian government to modify its approach towards Ukraine.

Specifically, the US Treasury Department's Office of Foreign Assets Control (OFAC) OFAC expanded the so-called "sectoral sanctions" previously issued under [Executive Order 13662](#) and first implemented by OFAC Directives 1 and 2 in July 2014. OFAC amended [Directive 1](#) and [Directive 2](#) to revise existing restrictions on dealing in new debt and equity covered by those directives. Most importantly, Directive 1 now restricts dealings in new debt of covered entities of greater than 30 days duration (decreased from 90 days). OFAC also added new entities to the list of those covered by Directives 1 and 2, including Sberbank, Russia's largest bank.

OFAC also issued new [Directive 3](#) and [Directive 4](#). Directive 3 imposes debt financing restrictions on Rostec, a Russian conglomerate operating in the defense and related materiel sector. Directive 4 prohibits the provision, exportation or reexportation — directly or indirectly — of goods, services (not including financial services) or technology to five Russian energy firms, if the export supports "exploration or production for Russian deepwater, Arctic offshore, or shale projects that have the potential to produce oil in the Russian Federation, or in maritime areas claimed by Russia and extending from its territory."

OFAC also designated and blocked the assets of five Russian state-owned defense technology firms.

Each of these OFAC sanctions measures is directed at activities of US persons, which includes companies organized under US law and their foreign branches, US nationals and US lawful permanent residents, and anyone physically present in the United States.

The EU expanded its Russia-related sanctions by adding to the list of entities denied access to the EU capital markets, broadening export controls and adding persons to the EU asset freeze list. The new EU sanctions are set out in [Council Regulation \(EU\) No. 960/2014](#) (the EU Regulation) and [Council Implementing Regulation \(EU\) No. 961/2014](#).

Services to the Russian Oil Industry

The amended US and EU sanctions now largely mirror each other in prohibiting the export of goods, services and technology in support of certain energy-related projects in Russia. Directive 4 prohibits US

persons from providing or reexporting —directly or indirectly — goods (presumably of any origin), 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 offshore areas claimed by the Russian Federation, and that involve the following five energy firms:

- Gazprom
- Gazpromneft
- Lukoil
- Rosneft
- Surgutneftegas

OFAC issued [Frequently Asked Questions](#) in conjunction with Directive 4 explaining that the prohibition on the exportation of services extends to drilling services, geophysical services, geological services, logistical services, management services, modeling capabilities and mapping technologies. The prohibition does not apply to the provision of financial services, *e.g.*, clearing transactions or the provision of insurance related to such activities.

Pursuant to a [General License](#) issued concurrently with Directive 4, US persons have until September 26, 2014, to wind down affected transactions with or relating to these Russian energy firms. The General License does not authorize the new provision, exportation or reexportation of goods, services (except for financial services) or technology except as needed to cease operations. OFAC requires a detailed report within 10 business days after wind-down activities conclude.

Although similar to the US export restrictions, the EU sanctions potentially apply more broadly. Whereas the earlier EU sanctions (in force since July 31, 2014) restricted exports of “technologies” to the Russian oil industry for use in deepwater, Arctic or shale oil projects in Russia, the EU Regulation now also extends to the export of services and encompasses service contracts related to drilling, well testing, logging and completion services, as well as the supply of specialized floating vessels in these oil industry sectors. The EU Regulation contains a grandfathering provision for service contracts executed before September 12, 2014, and a limited exception for services necessary for health and safety and environmental reasons.

Equity or Debt Financing for Certain Russian Banks

The US and EU sanctions that deny access to, respectively, the US and EU capital markets now target the following state-owned banks:

- Bank of Moscow (US only)
- Gazprombank
- Russian Agricultural Bank
- Sberbank
- Vnesheconombank
- VTB Bank

With respect to the US sanctions, OFAC’s revised Directive 1 tightens the debt financing restrictions applicable to the (now) six sanctioned Russian banks, reducing from 90 days to 30 days the maturity period for new debt subject to the prohibition. OFAC has also clarified that these debt financing restrictions include new extensions of credit through mechanisms such as deferred purchase agreements with entities covered by Directives 1, 2 or 3. Similarly, the EU Regulation reduces from 90 days to 30 days

the maturity period of transferable securities and money-market instruments subject to the restriction (so long as they are issued after September 12, 2014).

Debt Financing and Other Instruments Relating to Certain Russian Energy Companies

The US and EU sanctions are now closely aligned in denying the following energy companies access to the US and EU capital markets:

- Gazpromneft
- Novatek (US only)
- Rosneft
- Transneft

Under the US sanctions, OFAC's revised Directive 2 maintains the previous 90-day maturity period for new debt issued by listed Russian energy companies and adds two entities — Gazpromneft and Transneft — to the list of companies subject to this Directive. By contrast, the EU Regulation prohibits dealing in transferable securities and money-market instruments with a maturity exceeding 30 days issued after September 12, 2014, by Gazpromneft, Rosneft or Transneft, or their non-EU subsidiaries.

Debt Financing and Other Instruments Relating to Certain Companies in the Russian Defense Sector

The US and EU capital markets sanctions now apply to the following Russian defense companies:

- Rostec (US only)
- OPK Oboronprom (EU only)
- United Aircraft Corporation (EU only)
- Uralvagonzavod (EU only)

Under the US sanctions, OFAC's new Directive 3 prohibits transactions by US persons or within the United States involving new debt of greater than 30 days maturity issued by Rostec. The EU imposed a similar restriction on dealings in transferable securities and money-market instruments with a maturity exceeding 30 days issued by the three Russian defense companies above or their non-EU subsidiaries.

EU Restriction on New Loans and Credit, and Other Amendments to the EU Financial Sanctions

The EU Regulation further prohibits any arrangement, direct or indirect, "to make new loans or credit with a maturity exceeding 30 days" to any of the listed persons (*i.e.*, the EU-listed state-owned banks, defense entities and publicly owned oil companies) after September 12, 2014.

This prohibition is subject to important exceptions. It does not apply to loans or credit that are expressly and specifically intended to provide financing for non-prohibited imports or exports of goods and non-financial services between the EU and Russia, or to loans that are specifically intended to provide emergency funding to EU subsidiaries of the five state-owned banks that are denied access to the EU capital markets. Furthermore, Recital (6) of the EU Regulation states that the prohibition does not affect "deposit services, payment services, insurance services, loans from the institutions [listed under the debt and equity finance sanctions] and derivatives used for hedging purposes in the energy market." The term "credit" is not defined, however, and the EU Regulation has not clearly established the scope of this new measure.

The amended EU Regulation also includes amendments to certain terms implementing the capital markets restrictions. For example, the EU Regulation uses the expression “investment services,” presumably to ensure conformity with the *Markets in Financial Instruments Directive*.¹ However, the prohibition on the provision of “investment services” to listed entities remains broad, and includes, for example, “portfolio management,” “investment advice” and “placing of financial instruments without a firm commitment basis” — meaning that EU persons need to be vigilant if providing financial services to any of the listed entities.

Also, the amended EU Regulation has revised the definition of “transferable securities” falling within the sanctions’ scope. The new definition indicates that the listed classes of securities are exhaustive and include securities “giving the right to acquire or sell any such transferable securities” — excluding the further words “or giving rise to a cash settlement.” HM Treasury has provided no clarification in its [explanatory notice](#), so the EU’s reason for this revised definition remains unclear.

Blocking, Asset Freezes and Travel Bans

OFAC also added five Russian state-owned defense technology firms to its Specially Designated Nationals and Blocked Persons List (SDN List). As a result, US persons generally cannot deal with these firms and their property must be blocked if in the United States or in the possession or control of a US person. The parties added to the SDN List are:

- Almaz-Antey GSKB
- JSC NIIP
- Kalinin Machine Plant JSC
- Mytishchinski Mashinostroitelny Zavod OAO
- OAO ‘Dolgoprudny Research Production Enterprise’

The EU has also added 24 individuals to its asset freeze (listed in the Annex to [Council Implementing Regulation \(EU\) No. 961/2014](#)), and [Council Decision 2014/658/CFSP](#) requires EU Member States to restrict the travel of these individuals into or through EU territory. The newly designated individuals are identified as associated with the annexation of Crimea, the “Donetsk People’s Republic” or militias operating in eastern Ukraine.

Export Restrictions

The US and EU have also tightened restrictions on exports to Russia. The US Department of Commerce’s Bureau of Industry and Security (BIS) added to the [BIS Entity List](#) five entities in Russia’s defense sector and (depending on the activity) five entities in Russia’s energy sector. This move imposes a requirement to apply for a BIS license, which presumptively will be denied, if the exporter, reexporter or transferor knows that the exported items will be used directly or indirectly in exploration for, or production from, deepwater, Arctic offshore or shale projects in Russia. The energy companies added to the BIS Entity List are the same five listed under Directive 4 (Gazprom, Gazpromneft, Lukoil, Rosneft and Surgutneftegas).

The EU Regulation prohibits the export to certain Russian defense companies of dual-use goods as listed in Annex I of the EU Dual-Use Regulation (which establishes the common list of dual-use items that require authorization for export from the EU). The Russian entities covered by this restriction are listed in Annex IV. This prohibition also extends to the provision of related technical assistance, brokering services, financing or financial assistance.

This prohibition is subject to a grandfathering clause confirming that contracts concluded before September 12, 2014, are not affected, along with a provision that this prohibition shall be without prejudice “to the provision of assistance necessary to the maintenance and safety of existing capabilities within the EU.”

The EU Regulation further excludes from the prohibition’s scope exports of dual-use goods and technology intended for the “aeronautics and space industry,” or the related provision of technical and financial assistance, provided it is “for non military use and for a non military user,” as well as for “for maintenance and safety of existing civil nuclear capabilities within the EU”.

Potential for Additional Sanctions

We are continuing to monitor the implementation of these new measures and the potential for additional sanctions.

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¹ Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004.