Congress Readying Russia Sanctions: Implications for U.S. Nuclear Commerce

Aleksandar Dukic
Ari Fridman

June 28, 2017

Agenda

- Overview of Existing U.S. Russia Sanctions
- Summary of Russia Sanctions Legislation
- Political Overview
- Recent OFAC Ukraine-Related Designations
- Proposed Sanctions Provisions
- Implications for U.S. Nuclear Industry
- Q&A

Overview of Existing U.S. Sanctions on Russia

- Ukraine-/Russia-related Sanctions introduced in March 2014 as targeted sanctions focused on SDNs, but four Executive Orders in total
- Four key components:
  - Restrictions on dealing with SDNs
  - Sectoral sanctions under 4 Directives (target banks, oil/gas, and defense companies in Russia – each group is subject to different restrictions)
    - Restrictions on certain financial dealings (new debt / equity)
    - Restrictions on certain exploration or production projects in Russia
  - Export controls (the International Traffic in Arms Regulations, or ITAR, and Export Administration Regulations, or EAR)
  - Crimea (broad territorial sanctions, i.e. prohibition on exportation or importation of any goods, services, or technology to or from the Crimea region of Ukraine, as well as new investment in the Crimea region of Ukraine by a U.S. person, wherever located).

Overview of Existing U.S. Sanctions on Russia, cont'd.

- Treasury's Office of Foreign Assets Control ("OFAC") published the Sectoral Sanctions Identification List ("SSIL"), which identifies entities subject to these restrictions
  - Entities listed on the SSIL are not Specially Designated Nationals, or SDNs
  - SSIL restrictions apply to entities owned by SSIL entities at 50 percent or greater interest, directly or indirectly
  - Restrictions extend to evasion, conspiracy to violate, or causing a violation of these measures
- Complex financial restrictions, "debt" also includes extending payment terms to a designated party in excess of 30 or 90 days (depending on designation)
- Challenges in conducting due diligence in light of complex structures

Summary of Russia Sanctions Legislation

- On June 14, 2017, the Senate passed an Amendment to an Iran sanctions bill (S.722) that would expand sanctions against Russia and codify existing sanctions authority.
- This new legislation:
  - Does <u>not</u> specifically target nuclear-related activities, but it would result in a more complex business environment for companies dealing with Russia.
  - Expands restrictions on certain financial transactions and financial institutions that could cause Western banks to offer less financing for Russia-related transactions.
  - Would increase the number of and frequency of designations of Russian entities and individuals, making compliance with the Russian sanctions regime more challenging and complex.
- Though "mandatory," most of the provisions may be waived by the President for national security reasons and most are not self-executing.

Political Overview

- It is unclear whether the House will pass its own Russia sanctions bill.
- Even if the House does enact one, it may differ from the Senate package.
- White House may try to weaken the congressional review provision pertaining to lifting of sanctions.
- House leadership may try to better align itself with the current administration's preference for greater cooperation with Russia and more flexibility to raise and lower pressure on Russia in recognition of diplomatic progress.
- External pressures and status of Russia investigations can weigh on House leadership as well.
- We will continue to monitor the House closely for any significant new developments.

Recent OFAC Ukraine-Related Designations

- On June 20, OFAC designated 38 individuals and entities as SDNs and added 20 new SSIs under Ukraine-related authorities, including:
  - One entity that has engaged in the evasion of existing sanctions, two Russian government officials and two individuals acting for or on behalf of a government official, two entities that are owned or controlled by an individual previously designated, and 11 individuals and entities that operate in the Crimea region of Ukraine.
  - As a result of this action, any property or interest in property of the new SDNs in the possession or control of U.S. persons or within the United States must be blocked. Additionally, transactions by U.S. persons involving these persons are prohibited.
  - OFAC also identified 20 subsidiaries that are owned 50 percent or more by the previously-designated SSI, AK Transneft OAO (Transneft), subject to Directive 2, which prohibits U.S. persons from dealing in new debt of greater than 90 days maturity of the sanctioned entities.

Sanctions on Railway, Shipping, Metals, and Mining Sectors

- Section 223(a) would codify section 1(a) of Executive Order 13662, authorizing the designation of persons involved in a state-owned entity operating in the railway and shipping sectors of the Russian economy.
- The President already has authority under Executive Order 13662 to impose sanctions on persons in the metals and mining sector. In the future, the President could designate entities in Russian railway and/or shipping industries, making it tougher to transport goods to and from or within Russia.
- Regarding business with the mining and metals industries in Russia, mining would presumably include uranium mining, so potential future sanctions could affect state-owned companies engaged in uranium production.
- Like many other provisions, this one is not self-executing; instead, the U.S. government must designate companies that will be subject to sanctions.

Sanctions on Financial Services and Energy Sectors

1. Debt Financing for Financial and Energy Transactions

- *Requires* Department of Treasury to modify Directives 1 and 2 of the SSIL to make debt financing with certain designated Russian financial institutions and energy companies more difficult by reducing the length of the maturity date for debt financing (or other extension of credit) that a U.S. person can offer to, or otherwise facilitate for, a Russian financial institution or a Russian energy company designated under the directives.
- Currently no Russian nuclear entities are designated under the directives.

Sanctions on Financial Services and Energy Sectors, cont'd.

2. Restrictions on Unconventional Oil Projects

- Expands Directive 4 to prohibit U.S. persons from providing any goods, services (except for financial services), or technology in support of exploration or production for deepwater, Arctic offshore, or shale projects involving a designated Russian energy company, <u>regardless</u> of the location of the project.
- Such projects outside of Russia would also be prohibited, e.g. a project involving a designated Russian energy company engaging in one of these projects in Iraq or Venezuela would be subject to sanctions.

Sanctions on Financial Services and Energy Sectors, cont'd.

3. Financing for Russian Energy Infrastructure

- Authorizes the President to impose sanctions on a person who has:
  - (1) been determined to knowingly make an investment that directly and significantly contributes to the enhancement of the Russian Federation to construct energy export pipelines, or
  - (2) sells, leases, or provides to the Russian Federation, for the construction of Russian energy export pipelines, goods, services, technology, information, or support (any of which has a fair market value of $1 million or more, or that, during a 12-month period, has an aggregate fair market value of $5 million or more) that could directly and significantly facilitate the maintenance or expansion of the construction, modernization, or repair of energy pipelines by the Russian Federation.

Sanctions on Financial Services and Energy Sectors, cont'd.

4. Sanctions on Foreign Financial Institutions Facilitating Defense- and Energy-Related Transactions

– Amends Ukraine Freedom Support Act of 2014 to *require* the President to impose sanctions on foreign financial institutions determined to have knowingly facilitated certain defense- and energy-related transactions on behalf of the Russian Government.

Sanctions on Financial Services and Energy Sectors, cont'd.

5. Sanctions on Foreign Financial Institutions Facilitating Transactions with Designated Russian Persons

- *Requires* the President to impose sanctions on foreign financial institutions determined to have knowingly facilitated a significant financial transaction on behalf of any Russian person listed on Department of Treasury's SDN List. A national interest waiver is provided in this provision.
- Not self-executing: the President or his designee has the ability to exercise discretion and determine if institutions have engaged in such activities.
- The threat of designation likely will lead foreign financial institutions to be extremely cautious before engaging in any activities involving Russia that could create exposure for them under the new sanctions.

Sanctions Against Corruption and Divestment of State Assets

- Amends the Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014 to *require* the President to impose sanctions on persons in the Russian Federation complicit in or responsible for significant corruption.
- *Requires* the President to impose sanctions on persons determined to have knowingly made, or facilitated, an investment of $10 million or more if the investment directly and significantly contributes to the ability of the Russian Federation to privatize state-owned assets in a manner that "unjustly" benefits Russian Government officials or close associates or family members of those officials.
  - The terms "unjustly benefit" and "close associate" are not defined. A national security waiver is provided for these provisions.

Sanctions on Evaders and Human Rights Abusers

- Amends the Support for the Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014 to *require* the President to impose sanctions on foreign persons determined to have knowingly violated, or caused a violation of, any of the Russia-related Executive Orders or facilitated significant "deceptive or structured transactions" on behalf of persons (or close relatives) subject to sanctions imposed by the United States with respect to the Russian Federation.
- *Requires* the President to impose sanctions on a foreign person determined, "based on credible information," to be involved with human rights abuses in territory controlled by the Russian Federation.
- There is a national security interest waiver provided for these provisions, which also allows the President, or his designee, to exercise discretion in making the *required* determination before designating a party.

Sanctions on the Russian Intelligence and Defense Sectors

- *Requires* the President to impose sanctions on persons that have been determined to knowingly engage in a significant transaction with a person that is part of, or operates for or on behalf of, the defense or intelligence sectors of the Government of the Russian Federation, e.g. the Main Intelligence Agency of the General Staff of the Armed Forces of the Russian Federation or the Federal Security Service of the Russian Federation.
- There is a presidential waiver provided for in this section. As the statute does not provide further clarity as to what is meant to be "a part of" the defense or intelligence sectors, there could be reluctance on the part of U.S. and non-U.S. companies to engage in activities with entities in Russia that are even remotely related to these sectors.

Sanctions on Russian Cybersecurity Activities

- The President is *required* to impose sanctions on persons whom he has determined knowingly engaged in significant activities undermining cybersecurity against any person, including a democratic institution, or government on behalf of the Government of the Russian Federation.
- The President is also *required* to impose sanctions with respect to any person that he determines has knowingly materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services (except financial services) in support of the aforementioned cybersecurity activities.
- Finally, the President is *required* to impose sanctions with respect to any person that the President determines knowingly provided financial services in support of the aforementioned cybersecurity activities.

Implications for the U.S. Nuclear Industry

- Again, this legislation does not expressly target nuclear energy-related activities.
  - [NOT INCLUDED IN SENATE BILL] Section 209 of the Counteracting Russian Hostilities Act would authorize the President to impose sanctions on persons determined to knowingly make an investment in goods, services, technology, information, or support that could directly and significantly facilitate the maintenance or expansion of the construction, modernization, or repair of civil nuclear plants by the Russian Federation.
- Instead, it would codify and expand potential sanctions against industries indirectly related to the nuclear industry, which, in turn, would have implications for NEI members.
- For example, it would codify the President's authority to designate persons involved in state-owned entities operating in the railway, shipping, or metals and mining sectors of the Russian economy.
- To the extent the President designates entities in these industries, particularly mining and shipping, it could potentially become more difficult for U.S. companies to import uranium from Russia, and transport goods to and from or within Russia.

Implications for the U.S. Nuclear Industry, cont’d.

- **(De-Risking)** While expanded restrictions on financial transactions and financial institutions may not directly affect nuclear companies, these sanctions could result in greater de-risking by Western financial institutions and banks with regard to Russia, resulting in less financing being available for Russia-related transactions.
- **(Special Oil Projects)** Perhaps even more impactful, energy and other companies could be prohibited from providing goods, services or technology in support of unconventional oil projects anywhere in the world if a sanctioned Russian energy firm is involved (as opposed to the current sanctions that target only unconventional projects in Russia or its territorial waters).
- **(Party Screening)** Finally, the expanded sanctions *requiring* the President to designate foreign sanctions evaders, human rights abusers, and persons knowingly involved in the Russian defense and intelligence sectors may result in a significant increase in restricted party designations related to Russia, which would make conducting business involving Russia more complex and risky. U.S. companies doing business in Russia need to ensure that they have a robust restricted party screening process for Russia-related transactions.

Questions?

Aleksandar Dukic

+1 202 637 5449

aleksandar.dukic@hoganlovells.com

Ari Fridman

+1 202 637 5449

ari.fridman@hoganlovells.com