

# Senate Adopts New Sanctions Targeting Russia and Iran

June 16, 2017

On June 15, 2017, the United States Senate adopted S.722, incorporating the “Countering Russian Influence in Europe and Eurasia Act of 2017” and the “Countering Iran’s Destabilizing Activities Act of 2017,” by a vote of 98-2. The new law (the “Sanctions Bill”), assuming it is passed by the House and adopted, would:

- codify all existing Russia sanctions and designations (meaning the Trump Administration cannot unilaterally lift them) and require congressional review for any subsequent changes in licensing policy;
- tighten existing sectoral sanctions against Russian state-owned energy, financial, and defense companies and threaten their expansion to the state-owned shipping, rail, and mining/metal sectors;
- reinvigorate existing but currently unenforced secondary sanctions targeting Russia and add new secondary sanctions provisions targeting Russian pipeline transactions in particular (but leave those sanctions in the hands of the Trump Administration); and
- expand authority to sanction Russian cyber-related activities.

With respect to Iran, the Sanctions Bill would impose a largely symbolic expansion of secondary sanctions against Iranian military activity and sharpen focus on the Iranian Revolutionary Guard Corps and its affiliates.

The bill now proceeds to the House for consideration, the timing of which is uncertain, and it is possible that further amendments will be made. However, given the margin of passage of the Sanctions Bill and the bipartisan negotiations resulting in its adoption, it appears that there is a good chance that the final legislation passed by the House will be broadly similar and will be adopted by a margin sufficient to override any veto by President Trump.

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## RUSSIA/UKRAINE-RELATED SANCTIONS

### Codification of Existing Russian Sanctions.

The Sanctions Bill would codify all of the existing sanctions related to Russia's alleged activities in Ukraine and cyberattacks, meaning that only Congressional action can remove those sanctions.<sup>1</sup> Furthermore, any changes to licensing policy that would "significantly alter U.S. foreign policy," as well as any proposal to terminate or waive U.S. sanctions or return Russian access to diplomatic properties cut off during the Obama Administration, would have to be notified to Congress, with an opportunity to disapprove the relevant changes.<sup>2</sup>

### Modification of Current Sectoral Sanctions.

Pursuant to E.O. 13362, the Secretary of the Treasury is authorized to designate sectors of the Russian economy as potential sanctions targets. The Russian financial, energy, and defense sectors have been designated as eligible for sanctions, and OFAC has specified the limited sanctions applicable in Directives 1 through 4 and designated particular entities in those sectors to which they apply on the Sectoral Sanctions Identification List ("SSI List").

The Sanctions Bill modifies the sanctions applicable under Directive 1 (relating to the Russian financial sector) and Directive 2 (relating to the Russian energy sector), shortening the maximum permissible duration of new debt extended to designated entities. For designated SSI List entities in the financial sector, the maximum duration of new debt is cut from 30 days to 14 days; for entities in the energy sector, it is cut from 90 days to 30 days.<sup>3</sup>

The Sanctions Bill also expands the scope of Directive 4, which prohibits the provision, exportation, or reexportation, directly or indirectly, of goods, 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 involving designated persons. Previously, Directive 4 was limited to projects in the territory or exclusive economic zone of Russia; now, it applies to such projects worldwide if SSI List entities designated under Directive 4 are involved.<sup>4</sup> Moreover, as discussed below, the provision of financial services in support of investment in these projects may now be subject to secondary sanctions.

### Expansion of Secondary Sanctions

"Secondary sanctions" are U.S. sanctions programs that target activity by non-U.S. persons outside U.S. jurisdiction (as opposed to "primary" or "direct" sanctions, which require some act within U.S. jurisdiction, such as direct or indirect participation of U.S. persons, acts within the United States, or exports of U.S.-origin goods or services, including U.S. dollar clearing transactions). The enforcement mechanism is political rather than judicial; effectively, secondary sanctions threaten that if a foreign

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<sup>1</sup> S. 722, 115<sup>th</sup> Cong., § 222. Sanctions imposed under Executive Orders 13660, 13661, 13662, 13685, 13694, and 13757, together with all designations as of the day before final passage of the Sanctions Bill, would be codified.

<sup>2</sup> *Id.* § 216.

<sup>3</sup> *Id.* § 223(b)-(c).

<sup>4</sup> *Id.* § 223(d).

person engages in the targeted activity, the United States will add that foreign person to U.S. sanctions lists.

Typically, the sanctions available include designation as an SDN fully blocked from all interaction with the U.S. economy (“SDN sanctions”); imposition of a specified number of sanctions from a list of possible sanctions ranging from relatively mild (e.g., denial of export credit assistance) to severe (e.g., designation as an SDN) (“Menu-based sanctions”);<sup>5</sup> or, for financial institutions, barring or severely restricting the institution’s access to U.S. correspondent accounts, impairing its ability to do dollar-denominated transactions (“Correspondent account sanctions”).

### *Reinforcement of Existing Secondary Sanctions*

As noted in a prior memo,<sup>6</sup> the Ukraine Freedom Support Act of 2014 (“UFSA”) provided for secondary sanctions against, among others:

- any person making a “significant investment” in Arctic offshore, shale, or deepwater projects with the potential to produce oil in the territory or exclusive economic zone of the Russian Federation (Menu-based sanctions);<sup>7</sup> or
- any financial institution knowingly engaging in significant transactions relating to the sale of weapons to Syria or investment in Arctic offshore, shale, or deepwater projects in the Russian Federation with the potential to produce oil (Correspondent account sanctions); or
- any financial institution facilitating significant financial transactions for any person or entity designated as an SDN under Ukraine-related sanctions (Correspondent account sanctions).

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<sup>5</sup> Menu-based sanctions under the Sanctions Bill include five or more of the following: (1) denial of trade finance services from the Export-Import Bank of the U.S. for transactions involving the sanctioned person; (2) denial of export licenses for exports to the sanctioned person; (3) prohibition on U.S. banks lending more than \$10 million in any 12-month period to the sanctioned person; (4) U.S. opposition to any loan from an international financial institution, (5) blocking a financial institution from serving as a primary dealer in U.S. government debt instruments or serving as a depository of government funds; (6) a bar on U.S. government procurement; (7) prohibition on any transaction in foreign exchange that are subject to U.S. jurisdiction; (8) prohibition on any transfer of credit or payment through the U.S. financial system in which the sanctioned person has an interest; (9) blocking all property within U.S. jurisdiction in which the sanctioned person has an interest; (10) prohibition on U.S. persons’ investing in equity or debt of the sanctioned person; (11) visa bans on corporate officers and controlling shareholders; or (12) imposition of any of the sanctions above on the principal executive officers of the sanctioned person. S. 722, 115<sup>th</sup> Cong., § 235.

<sup>6</sup> See [Ukraine-related Sanctions: New U.S. Statute Creates Secondary Sanctions Targeting Certain Dealings with Russia](#) (Dec. 17, 2014).

<sup>7</sup> Menu-based sanctions under UFSA include three or more of the following: (1) prohibition of assistance from the Export-Import Bank of the United States; (2) prohibition against procurement of goods and services by United States executive agencies; (3) prohibition of provision of defense goods and services to the sanctioned foreign person or entity; (4) prohibition of licensing of arms and other dual-use exports for the benefit of the sanctioned foreign person or entity; (5) prohibition against engaging in certain U.S. property transactions, but not including the authority to restrict the importation of goods; (6) prohibition against certain banking transactions, including transfers of credits and payments involving an interest of the sanctioned foreign person or entity; (7) prohibition of certain investments by U.S. persons in equity and debt transactions involving the foreign person; (8) exclusion of foreign sanctioned persons from the United States and revocation of visas or other documentation; and (9) imposition of any of the aforementioned sanctions against the executive officers of a foreign sanctioned entity. Ukraine Freedom Support Act of 2014, Pub. L. No. 113-272, 128 Stat. 2952, § 4.

Shortly after the passage of UFSA, the Obama Administration indicated that it had no current intention to use the secondary sanction authority, which at the time was permissive only.<sup>8</sup> However, the imposition of sanctions against persons engaged in targeted activities is now “mandatory.”<sup>9</sup> As a practical matter, the Trump Administration still has to take affirmative action to impose sanctions upon individuals or entities engaged in the targeted conduct, but the political pressure to do so may increase, and the validity of the previous statement of intent not to enforce is now questionable.

The Sanctions Bill also reinforces existing secondary sanctions against corruption, making mandatory the imposition of SDN sanctions against “any official of the Government of the Russian Federation, or a close associate or family member,” who is responsible for “acts of significant corruption” in the Russian Federation or elsewhere as well as any person who has “materially assisted, sponsored, or provided financial, material, or technological support for” such corruption.<sup>10</sup>

### *Expansion of Secondary Sanctions*

The Sanctions Bill also establishes a number of new secondary sanctions programs, all of which are also styled as “mandatory.” Targeted persons include those who do any of the following:

- Knowingly facilitate significant “deceptive” or “structured” transactions on behalf of any person subject to US Ukraine-related or cybersecurity sanctions, or a child, parent, spouse, or sibling of a sanctioned person (SDN sanctions). “Deceptive” transactions conceal the interest of a sanctioned person from any participant or regulator, and “structured” transactions are broken down into small amounts to avoid AML controls. The deceptive transactions provision appears to apply to transactions concealing the role of SSI List entities as well as to SDNs;<sup>11</sup>
- Knowingly engage in any significant transaction with a person that is part of, or operates for or on behalf of, the defense or intelligence sectors of the Russian Federation (Menu-based sanctions);<sup>12</sup>
- Knowingly invest in Russian energy export pipelines in an amount exceeding \$1 million in any transaction or \$5 million over any 12-month period (Menu-based sanctions);<sup>13</sup>
- Knowingly provide goods, services, or technology for any Russian energy pipeline, whether or not for export (Menu-based sanctions);<sup>14</sup>
- Engage in, direct, or be complicit in serious human rights abuses in territory controlled by the Russian Federation, or materially assist, sponsor, or provide material, financial, or technological support for, or goods or services to, such a person (SDN sanctions);<sup>15</sup>

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<sup>8</sup> “Statement by the President on the Ukraine Freedom Support Act” (Dec. 18, 2014), *available at* <https://obamawhitehouse.archives.gov/the-press-office/2014/12/18/statement-president-ukraine-freedom-support-act>.

<sup>9</sup> S. 722, 115th Cong. §§ 225, 226.

<sup>10</sup> *Id.* § 227; *see also* 22 U.S.C. § 8908(a) (2014).

<sup>11</sup> S. 722, 115th Cong. §228.

<sup>12</sup> *Id.* § 231(a).

<sup>13</sup> *Id.* § 232.

<sup>14</sup> *Id.*

<sup>15</sup> *Id.* § 228; *See also* 22 U.S.C. § 8901 et seq. (2014).

- Knowingly engage in significant activities undermining cybersecurity against any person, including any government or democratic institution, on behalf of the Government of the Russian Federation (SDN sanctions);<sup>16</sup>
- Knowingly materially assist, sponsor, or provide financial, material, or technological support for, or goods or services in support of, the foregoing activities undermining cybersecurity (Menu-based sanctions);<sup>17</sup>
- Knowingly invest more than \$10 million, individually or in an aggregate of transactions of at least \$1 million in any 12-month period, or facilitate such an investment, if it “directly and significantly contributes to the ability of the Russian Federation to privatize state-owned assets in a manner that unjustly benefits” Russian officials or their close associates (Menu-based sanctions);<sup>18</sup> and
- Knowingly provide to Syria significant financial, material, or technical support that contributes materially to Syria’s ability to acquire or develop weaponry, particularly weapons or mass destruction (SDN sanctions).<sup>19</sup>

### *Impact of Secondary Sanctions*

It remains to be seen whether the marked expansion of secondary sanctions programs targeting Russia will have a significant impact. Such programs did influence international behavior with respect to Iran, but most of the sanctions here (aside from the new sanctions targeting pipelines) relate to activities of lesser commercial importance. It is also unclear how market participants will assess the risk of the Trump Administration (or future administrations) taking affirmative action to designate non-U.S. parties under these authorities.

### Reports & Strategy

The Sanctions Bill calls for a number of reports, notably on:

- Russian oligarchs and parastatal entities of the Russian Federation;
- The effects of expanding sanctions to target sovereign debt and derivative products;
- Illicit financial flows in and out of Russia, and Russian influence on European or Eurasian elections; and
- Media organizations controlled and funded by the Government of the Russian Federation.

None of the reports will result directly in action to expand sanctions, but they may indicate potential areas of interest for future proposals.

### **IRAN SANCTIONS**

The Sanctions Bill is notable primarily for being the first legislative expansion of Iranian sanctions since the JCPOA nuclear agreement was implemented. The sanctions are focused on Iranian ballistic missile

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<sup>16</sup> *Id.* § 224.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.* § 233.

<sup>19</sup> *Id.* § 234.

programs and support for terrorism, and their practical impact is limited given that comprehensive direct U.S. sanctions against Iran remain in place.

The new sanctions would:

- Target for secondary sanctions any person who knowingly engages in any activity that materially contributes to the Government of Iran’s ballistic missile program or other programs capable of delivering weapons of mass destruction (SDN sanctions);
- Require the President to designate the IRGC and foreign persons that are its officials, agents, and affiliates as SDNs under Executive Order 13224 (relating to terrorism); the IRGC is already an SDN under several other programs;
- Provide additional authority to designate persons responsible for gross violations of human rights in Iran against persons exposing illegal activity or advocating for human rights; such authority already exists; and
- Provide for secondary sanctions on any person who “knowingly engages in any activity that materially contributes to the supply, sale, or transfer directly or indirectly to or from Iran” certain major weapons systems (SDN sanctions).

These sanctions largely overlap existing authorities and seem intended as a political statement that the U.S. is still concerned about and applying pressure regarding Iran’s ballistic missile, terrorism, and regional military activities. There is no direct impact on the JCPOA, and given the modest practical impact it seems that significant political consequences are also unlikely.

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