

## International Trade Alert

October 30, 2017

### Key Points:

- On October 27, 2017, the U.S. State Department issued guidance identifying 39 entities related to the defense and intelligence sectors of the Government of the Russian Federation and issued related guidance on criteria to be used in identifying sanctionable “significant transactions.”
- Under Section 231 of the Countering America’s Adversaries Through Sanctions Act of 2017 (CAATSA or the “Act”), by January 29, 2018, President Trump is required to impose sanctions (or waive the application of sanctions) on those U.S. and non-U.S. persons who engage, or have engaged, in “significant transactions” with these entities since CAATSA was enacted on August 2, 2017.
- Punitive sanctions under these provisions of CAATSA include prohibitions on financing and financial services by certain public financial institutions, restrictions on debt and extensions of credit by other U.S. financial institutions, restrictions on other financial and property transactions, restrictions on investments in a sanctioned entity and restrictions on U.S. export licensing.
- In light of these new U.S. sanctions measures, companies with potentially affected interests in Russia should review their commercial relationships and commitments for possible risk exposure associated with the Russian entities identified by the State Department.



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### U.S. State Department Issues Belated List and Guidance on Extraterritorial Sanctions Affecting Russian Defense and Intelligence Sector Entities

On October 27, 2017, three weeks after the congressionally mandated deadline of October 1, the U.S. State Department issued guidance to Congress identifying 33 entities that are part of, or operating for or on behalf of, the defense sector of the government of the Russian Federation, as well as six entities that are part of, or operating for or on behalf of the intelligence sector of the government of the Russian Federation. This list provides the basis for U.S. sanctions action against companies found to engage in a “significant transaction” with the listed entities, which the Trump administration is required to implement by January 29, 2018.

## Background

President Trump signed the CAATSA legislation into law on August 2, 2017. Section 231 of this law requires the imposition of sanctions on anyone “that the President determines knowingly . . . engages 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, including 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.”

Although Section 231(a) provides for a delay in implementation and imposition of specific sanctions measures for 180 days after August 2, 2017, Section 231(d) requires that “[n]ot later than 60 days after the date of the enactment of this Act, the President shall issue regulations or other guidance to specify the persons that are part of, or operate for or on behalf of, the defense and intelligence sectors of the government of the Russian Federation.” This 60-day deadline expired on October 1, 2017.

Several members of Congress, on both sides of the aisle, publicly voiced concerns about the Trump administration’s commitment to implement these measures on a timely basis. In particular, Sen. John McCain, Chairman of the Senate Armed Services Committee, and Sen. Ben Cardin, Ranking Member of the Senate Foreign Relations Committee, wrote a letter to President Trump two days before the October 1 deadline reminding him of its imminence, and both senators were highly critical when the deadline passed with neither action nor explanation. More recently, Sen. Bob Corker, Chairman of the Senate Foreign Relations Committee, also voiced concern about the delay.

## Summary of Section 231 Provisions

Two days before the October 1 deadline, on September 29, 2017, President Trump delegated the authority to implement Section 231(d) of CAATSA, requiring the issuance of regulations or other guidance to specify persons that are part of, or operating for or on behalf of, the Russian defense and intelligence sectors to the Secretary of State in consultation with the Secretary of Treasury. As a first step in implementing these provisions, on October 27, 2017, the State Department issued a list of 39 entities that it identifies as part of, or operating for or on behalf of, the defense and intelligence arms of the Russian government.

### Targeted Russian Entities

Among other significant Russian companies on this list, it includes Rostec (Russian Technologies State Corporation), a Russian holding company active in the defense sector; Rosoboronexport JSC, Russia’s largest arms exporting company; and Kalashnikov Concern, a combat weapons producer. Certain entities listed, such as Sukhoi Aviation JSC, engage in both civilian as well as defense-related businesses. The list includes both state-owned enterprises as well as privately held companies (or subsidiaries of public companies). Additionally, some of the listed entities are subsidiaries of other entities that are included in the list. Some, but not all, of the entities listed are subject to U.S. sanctions imposed under other authorities. The full list may be viewed [here](#).

### **Punitive Sanctions Measures Applicable under Section 231**

Beginning on or after January 29, 2018, CAATSA requires the imposition of five or more of the following sanctions on companies determined to have engaged in a “significant transaction” in violation of Section 231 since August 2, 2017, unless the President waives or delays the initial imposition of these measures:

- restrictions on the provision of loans or providing credit totaling more than \$10 million in any 12-month period to a targeted entity by U.S. financial institutions
- a requirement that the United States oppose any loan from international financial institutions that would benefit a sanctioned person
- if the person is a financial institution, sanctions include:
  - prohibition by the Federal Reserve from being designated as a primary dealer in U.S. government debt instruments
  - prohibition from serving as an agent of the U.S. government or from serving as repository for U.S. government funds
- a prohibition on engaging in any transactions in a foreign exchange that is subject to U.S. jurisdiction
- restrictions on banking transactions by the sanctioned person, including transfers of credit or payments between, by, through or to any financial institution
- denial of approval for extensions of credit to a targeted entity by the U.S. Export-Import Bank
- denial of licenses to receive exports of controlled goods or technology from the United States
- a prohibition from engaging in U.S. government contracting
- a prohibition on transactions involving the property of the sanctioned person that is subject to U.S. jurisdiction
- a ban on investment by any U.S. person in the equity or debt of the sanctioned person
- denial of entry visas to the United States for foreign officers, principals and controlling shareholders of the sanctioned person
- the application of any of the above sanctions on the principal executive officer(s) of the sanctioned person.

Imposition of sanctions under the Section 231 provisions is due to begin on or after January 29, 2018. The State Department has stated that it will make such sanctions determinations and publish a related notice of such actions when this occurs. However, it has not otherwise indicated what the procedure will be or how such determinations will be made in practice.

### **Guidance and Criteria for Identifying Sanctionable “Significant Transactions”**

The State Department has also provided FAQs explaining what kinds of transactions might trigger sanctions under CAATSA in the coming months. In determining whether a transaction with a listed entity is “significant” for purposes of Section 231 of CAATSA, the State Department will consider “the totality of

the facts and circumstances surrounding the transaction and weigh various factors on a case-by-case basis.” Factors considered may include (i) the significance of the transaction to the U.S. national security and foreign policy interest and, in particular, whether it has a significant adverse impact on such interests; (ii) the nature and magnitude of the transaction; and (iii) the relation and significance of the transaction to the defense or intelligence sector of the Russian government.

Initially, the State Department has indicated that it expects to focus on “significant transactions of a defense or intelligence nature” with those named on the list. However, not all transactions with the named entities will necessarily be subject to sanctions, particularly those transactions that have “purely civilian end-uses and/or civilian end-users, and do not involve entities in the intelligence sectors.” This FAQ suggests that sanctions may be aimed at specific activities or transactions undertaken by or with such entities. Importantly, the FAQs explain that the guidance is not a determination regarding imposition of sanctions, as no asset freezes or other sanctions are being imposed on any entity on the list, nor does inclusion on the list necessarily mean that such persons will be added to any one of the U.S. Department of the Treasury, Office of Foreign Asset Control’s (OFAC) sanctions lists.

The FAQs expressly state that if a transaction is necessary to comply with rules and regulations administered by the Federal Security Service (FSS) (including for the importation, distribution or use of information technology products in Russia, and the payment of any related fees to FSS) these factors will weigh “heavily” against a determination that such a transaction is “significant.” Moreover, on February 2, 2017, OFAC issued [Cyber-related General License No. 1](#), a general license that authorizes U.S. persons to engage in the aforementioned activities with the FSS.

The FAQs also address the issue of an allied or partner state that purchases Russian-origin military equipment, spare parts and related supplies, noting that the State Department intends to work with our allies and partners “to help them identify and avoid engaging in potentially sanctionable activity while strengthening military capabilities used for cooperative defense efforts.” During a press briefing on this guidance on October 27, 2017, in response to questions about the impact on allies who have Russian military equipment and may need to buy spare parts, a senior State Department official further emphasized the significance threshold that “would presumably exclude certain things that are less than significant” and added that the State Department would “consider the totality of circumstances in any individual case when making a decision, but I think that smaller-scale things, lesser things, would cut against making a decision that those are significant, particularly in cases where you have an ally that we want to have strong military capabilities to continue to partner with them across a range of scenarios.”

### **Congressional Reaction**

Members of Congress have reacted to this action by the administration by describing it as progress in implementing U.S. sanctions. At the same time, it is clear that Congress will continue to monitor closely, and press the administration to further enforce, the sanctions going forward. In a joint statement on October 26, 2017, Sens. McCain and Cardin commented that Congress “will continue to conduct oversight of each step [of the statute’s implementation] to ensure that the administration is following both

the letter and the spirit of the law – including persuading entities to stop doing business with those on the list, coordinating with European allies and other key partners, and briefing and consulting Congress on a regular basis.” In a separate statement, Sen. Corker added that the guidance “is a good first step in responsibly implementing a very complex piece of legislation” and that “Congress will expect thorough and timely consultation until full implementation is complete.”

### **Review and Consideration of Potential Risk Exposure**

It remains to be seen what practical impact the new measures will have on companies. In Europe, it is important to note that member countries of the European Union maintain defense-related restrictions that target exports of dual-use items and related technical and financial assistance to Russia and particular companies in the Russian defense sector. Moreover, many EU countries generally will not issue licenses for exports of dual-use items to entities in the Russian intelligence sector. Accordingly, this may limit the practical impact of the new U.S. measures on European companies. It is less clear how this will affect companies elsewhere.

At this time, it is important for companies that may be affected by these new U.S. sanctions measures to conduct careful diligence to identify any business that they may have with any of the 39 listed Russian defense and intelligence-related entities and determine implications for their interests and steps they may be required to take to comply with new U.S. sanctions restrictions expected to be imposed in January 2018. Companies should promptly assess transactions and interactions with such entities in light of this guidance to determine whether those transactions and interactions could be viewed as “significant,” potentially exposing such companies (including U.S. persons) to sanctions. Where risks are identified, it will be important to further evaluate practical options to address related concerns and obtain further guidance, including potential options to seek further guidance and consultation with U.S. officials on how the Section 231 provisions may apply, whether in direct communications or on a blind-basis, in consultation with U.S. Counsel.

## Contact

If you have any questions concerning this alert, please contact the lawyers listed below or any of Akin Gump's [Export Controls and Economic Sanctions partners](#).

**Wynn Segall**

[wsegall@akingump.com](mailto:wsegall@akingump.com)

+1 202.887.4573

Washington, D.C.

**Jasper Helder**

[jasper.helder@akingump.com](mailto:jasper.helder@akingump.com)

+44 20.7661.5308

London

**Jonathan Poling**

[jpoling@akingump.com](mailto:jpoling@akingump.com)

+1 202.887.4029

Washington, D.C.

**Nnedinma Ifudu Nweke**

[nifudu@akingump.com](mailto:nifudu@akingump.com)

+1 202.887.4013

Washington, D.C.

**Melissa J. Schwartz**

[mjschwartz@akingump.com](mailto:mjschwartz@akingump.com)

+1 202.887.4539

Washington, D.C.

**Chiara Klau**

[chiara.klau@akingump.com](mailto:chiara.klau@akingump.com)

+44 20.7661.5342

London

**Andrew Schlossberg**

[aschlossberg@akingump.com](mailto:aschlossberg@akingump.com)

+1 202.887.4314

Washington, D.C.