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US Secondary Sanctions Against Russia: Amidst Rising Tensions, Are Arbitral and Financial Institutions At Risk?

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This entry is the last in a series of three regarding issues faced by arbitral and financial institutions as a result of restrictions on transfers of funds under primary and secondary sanctions programmes. In the **first post**, the authors addressed the impact of asset freezes on arbitral institutions and their banks, while the **second post** dealt with some of the challenges that such institutions may experience as a result of restrictions that form part of the United States' ("US") secondary sanctions against Iran. This final post discusses the potential effects of US secondary sanctions against Russia on arbitral and financial institutions.

US Secondary Sanctions Against Russia Related to the Occupation of Crimea

The US maintains extensive sanctions against Russia, including sanctions imposed in response to alleged foreign election interference and other malicious cyber-enabled activities, human rights abuses, weapons proliferation and illicit trade with North Korea. The present post focuses on the US sanctions imposed against Russia following the Russia's 2014 occupation and annexation of the Crimea region in Ukraine, where tensions have recently **flared up** once again.

Most sanctions in respect of the Russian occupation of Crimea do not target the Russian state directly. They rather consist of designations of specific individuals, companies and other entities on the **SDN List** maintained by the Office of Foreign Assets Control ("OFAC") of the US Department of the Treasury. As noted in our **previous post**, the SDN List contains individuals and entities whose assets are blocked, primarily as a result of the fact that these individuals and entities are acting for or on behalf of, or are owned or controlled by, a target state. By September 2021, the US had designated about 735 persons and entities on the basis of Ukraine-related sanctions.[1)]

The US sanctions regime against Russia in respect of its occupation of the Crimea region is primarily based on a series of four Executive Orders ("EO") issued by President Obama in 2014, namely **EO 13660 of 6 March 2014**, **EO 13661 of 16 March 2014**, **EO 13662 of 20 March 2014** and **EO 13685 of 19 December 2014**. These EOs are based on national emergency statutory authorities and provide the framework for sanctions to be imposed on persons and entities the President determines are responsible for or complicit in, directly or indirectly, undermining democratic processes or institutions in Ukraine, illegally asserting governmental authority over any part of Ukraine or misappropriating Ukrainian state assets.

EO 13660 authorises the imposition of blocking sanctions against individuals and entities responsible for, *inter alia*, violating the sovereignty and territorial integrity of Ukraine or for actions or policies that threaten the peace, security, stability, sovereignty or territorial integrity of the country, while EO 13661 provides for blocking sanctions and travel restrictions against Russian government officials and persons operating in the Russian arms sector. EO 13662 in turn authorises sanctions against individuals and entities that operate in key sectors of the Russian economy, including the financial services, energy, metals and mining, engineering and defense sectors. Finally, EO 13685 prohibits US business, trade or investment in the Crimea region and authorises the imposition of blocking sanctions against those persons that the President determines have operated in, or been the leader of an entity operating in, Crimea.

Each of these EOs also authorises the imposition of blocking sanctions against any person that has materially assisted, sponsored, or provided financial, material or technological support for, or goods or services to or in support of, any person whose property and interests in property are blocked pursuant to the relevant EO.[2)]

In addition to the four Ukraine-related EOs, Congress passed, in 2014, two acts establishing sanctions in response to Russia's invasion of Ukraine: the **Ukraine Freedom Support Act of 2014** ("UFSA") and the **Support for the Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014** ("SSIDES").

On 2 August 2017, President Trump signed into law the **Countering America's Adversaries Through Sanctions Act** ("CAATSA"), which includes further sanctions with respect to the Russian Federation. Among other things, this piece of legislation amends the UFSA and the SSIDES, codifies the abovementioned Ukraine-related EOs and identifies several new targets for sanctions.

Do the Activities of Arbitral Institutions and their Banks Fall Within the Scope of US Secondary Sanctions Against Russia?

Compared to the often broad and comprehensive US secondary sanctions regime against Iran discussed in **the authors' previous post**, sanctions in respect of the Russian occupation of the Crimea region are more targeted.

That said, from a secondary sanctions perspective, section 5 UFSA and section 10 SSIDES, both as amended by CAATSA, have the potential to create significant compliance challenges for non-US persons and entities that engage in certain transactions with sanctioned Russian parties.

Pursuant to section 5(b) UFSA (as amended by section 226 CAATSA), a foreign financial institution risks the termination or restriction of access to its US correspondent and payable-through accounts ("CAPTA sanctions") if it is determined that it knowingly facilitated a significant financial transaction on behalf of any Russian person or entity included in the SDN List pursuant to the UFSA, EO 13660, EO 13661, EO 13662 or any other EO addressing the crisis in Ukraine.

OFAC will generally interpret the term "financial transaction" broadly to encompass any transfer of value involving a financial institution, including the receipt or origination of wire transfers, while "facilitated" is equally interpreted broadly and includes the provision of assistance for

certain transactions, including the transmission of value.[3] OFAC considers the totality of the facts and circumstances when determining whether a financial transaction is "significant."[4]

In addition, on the basis of section 10(a)(2)(A) SSIDES (as amended by section 228 CAATSA), non-US persons and entities risk being designated as SDN and face blocking sanctions if they are determined to have knowingly, on or after 2 August 2017, "*facilitate*[d] *a significant transaction or transactions, including deceptive or structured transactions, for or on behalf of* […] *any person subject to sanctions imposed by the United States with respect to the Russian Federation*."

Similar to the guidance provided in respect of section 226 CAATSA, facilitating a transaction for or on behalf of a person is understood to mean providing assistance for a transaction from which the person in question derives a particular benefit of any kind, which includes the transmission of financial instruments or any other value.

To date, the UFSA and the SSIDES have rarely been cited as independent authority for designations or other sanctions actions.[5]

That said, even if this appears unlikely, it cannot be excluded, on the basis of the guidance provided by OFAC, that the processing and acceptance of a transfer of funds from a sanctioned Russian party by a bank (such as the payment of a registration fee or of an advance on costs), might expose the latter to secondary sanctions pursuant to section 5(b) UFSA and section 10(a)(2) SSIDES. From the perspective of a non-US financial institution, even the slightest risk of CAPTA or blocking sanctions might justify refusing the transaction altogether.

Similarly, the likelihood that an arbitral institution end up in the crosshairs of OFAC appears to be low. *Prima facie*, administering a dispute in which one of the parties is subject to US sanctions against Russia does not appear to constitute the facilitation of a significant transaction for or on behalf of such sanctioned person or entity.

However, it is difficult to predict how OFAC will implement its arsenal of secondary sanctions in the future, in particular considering that **lingering geopolitical tensions in the relationship between Ukraine, Russia and the US** may lead the Biden administration to take a more stringent approach in respect of the enforcement of existing or new measures against Russia.

Furthermore, unlike provisions of the US sanctions programme against Iran related to the authorised supply of legal services, which make reference to arbitration proceedings conducted outside the US, the authorisation related to legal services under the Ukraine-related sanctions programme does not contain any such reference.[6] Therefore, should the administration of arbitration proceedings be deemed to amount to a facilitation of "*a significant transaction or transactions* […] *for or on behalf of*" a designated person or entity,[7] the relevant arbitral institution might be required to secure a specific license. For that reason, the threat of secondary sanctions continues to constitute a non-negligible risk for arbitral institutions and their banks when dealing with Russian parties and/or certain sectors of the Russian economy. Enhanced due diligence remains the norm.

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References

?1 Dianne E. Rennack/Cory Welt, *S. Sanctions on Russia: An Overview* (IF10779), Congressional Research Service, 1 September 2021, p. 1.

?2 *See* section 1(a)(iv) of EO 13660 dated 6 March 2014, section 1(a)(ii)(D) of EO 13661 dated 16 March 2014, section 1(a)(ii) of EO 13662 dated 20 March 2014 and section 2(a)(iv) of EO 13685 dated 19 December 2014.

?3 OFAC, *Frequently Asked Questions*, n. 542.

?4 OFAC, *Frequently Asked Questions*, nn. 542 and 545.

?5 Cory Welt/Kristin Archick/Rebecca M. Nelson/Dianne E. Rennack, *S. Sanctions on Russia* (R45415), Congressional Research Service, 17 January 2020, p. 13.

?6 See 31 CFR § 589.506.

?7 For instance, if the parties to an arbitration reach a settlement agreement, which might then be recorded in the form of an award made by consent of the parties in accordance with Article 33 of the ICC Rules of Arbitration.

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