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PRIMER: US and EU sanctions against Russia

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The new Russia Sanctions Bill, set to be debated in the US Congress in the coming weeks, has received criticism from the EU, suggesting that coordination between the two jurisdictions over Russia is over.

There is fear that the bill will impact companies financing the new Nord Stream 2 pipeline which carries natural gas from Russia to Germany. EU president Jean-Claude Juncker said that action will be taken if assurances are not given about protecting European companies from penalties. The extra-territorial effect of US sanctions means that European courts would have little choice but to accept the legislation.

Following the Russian invasion of Crimea in 2014, EU and US leaders began to impose sanctions on Russian and Ukrainian individuals closely connected to the Russian leadership, freezing funds and enforcing travel restrictions on these individuals. Further sanctions followed after Russia was accused of conducting cyberattacks on the US and interfering with the 2016 presidential campaign.

The environment between the US and Russia means other sanctions, or at least extensions of existing sanctions, are possible. This week, the EU extended sanctions until mid-2019 which impose travel bans and asset freezes on 155 people and 38 companies over Russia's annexation of Crimea and support for pro-Moscow rebels in eastern Ukraine.

There are not many alternatives for the EU and the US if political tensions escalate. The so-called nuclear option is to exclude

Russia from financial markets, forcing market participants to alternative payment systems and severely hindering Russian's ability to conduct global business.

What has been done so far?

The sanctions implemented are relatively targeted and there have been several phases affecting certain sectors of the Russian economy and specific transactions. Developments have been unprecedented, including adding oligarchs to the US specially designated nationals and blocked persons (SDN) list which effectively gives them only two options – keep control and cripple their businesses or get rid of their ownership to keep the business afloat.

"The sanctions are fairly targeted, despite the general perception that you cannot do any business in Russia"

Oleg Deripaksa has chosen to do the latter. The aluminium magnate and close ally of Russian President Vladimir Putin has decided to sell off part of his two-thirds stake in Russian energy company EN+ Group, after being added to the SDN list. The company faces the prospect of being barred from trading in US dollars and American companies are no longer allowed to deal with the energy company. Deripaska also controls aluminium company Rusal, also sanctioned, and US investors are banned from any dealing with the firm and other sanctioned entities. This has led Rusal to warn that the sanctions could trigger a default on debts.

After the wave of sanctions in August, Russian oligarchs were said to have lost almost \$12 billion in 24 hours.

"The sanctions are fairly targeted, despite the general perception that you cannot do any business in Russia," said Ashurst partner Sergei Ostrovsky. "They are limited to specific persons, sectors and transactions and are not as broad and all-encompassing so as to make it legally impossible to do any business in that country."

The sanctions enforced in 2014 restricted business with Russian oil and defence firms and companies supplying goods and technology which could be intended for military use in Russia. They also strengthened restrictions on Russia's access to EU capital markets.

The Office of Foreign Assets Control (Ofac) sanctions in 2018 imposed sanctions on seven so-called Russian business oligarchs and 12 companies they own, plus 17 Russian government officials and a Russian weapons company. These sanctions once again concerned travel bans and asset freezes, forbidding US persons from providing funds and forcing them to block their assets.

Yet despite the precise focus of the sanctions, in reality, these are having a big impact across all sectors in Russia.

"The general perception is that the appetite for Russian transactions from EU and US-based countries is limited, despite the fact that these could comply legally," Ostrovsky said.

Are there differences between the US and the EU's sanctions?

The US and the EU's approach is reasonably well aligned, but there are some crucial differences.

Section 228 of the Countering America's Adversaries Through Sanctions Act (CAATSA) applies to US persons but also foreign persons if they facilitate a significant transaction with anyone sanctioned. This means that these have an extra-territorial effect and therefore non-EU courts will have to make a judgement on whether the accused is doing a deal on behalf of a person sanctioned in the US.

If so, then any foreign person who violates sanctions imposed upon a Russian listed on the SDN is themselves at risk of being subject to US sanctions. This significantly limits Russians ability to conduct business globally. As yet there have been no test cases to see how this would be enforced.

Yet, while there may be differences, the high level of integration between the UK and the US means that from a practical risk perspective it does not make much of a difference, especially given the extra-territorial reach of the recent American sanctions legislation. "In general, people are being very cautious", said Ostrovsky.

According to Ropes & Gray US partner Ama Adams, the US sanctions are slightly broader than their EU counterparts. Last month the US was reported to be pushing Europe to adopt more stringent sanctions, but fears that the new proposed US sanctions could impact the new €9.5 billion (\$11.1 billion) Nord Stream 2 gas pipeline is making the EU resist strongly.

France said the Bill is unlawful due to its extraterritorial effect, which effectively means European courts would to accept the measures.

The US enacted sanctions in 2014 under two executive orders passed by the Obama administration. Concerns about President Trump's relationship with the Russian regime following the 2016 Presidential campaign and fears that he may be too lenient in his reproach of Russia, have led Congress to pass legislation to convert executive orders into law, so only they can change the law.

For the EU sanctions are applied on a pan-European basis, but penalties are up to each member state. The UK under The Ukraine (European Union Financial Sanctions) (No.2) Regulations 2014 could sentence any offender to two years in prison and anyone conducting business with designated persons must supply any relevant documentation to the HM Treasury and co-operate with verifying any information.

What other options do the EU and the US have?

US extending Russian sanctions could cause the EU to use laws to block these measures against European companies and individuals or impose outright bans on doing business with US companies. Trump's time in office suggests that they are unlikely to back down.

If Russian tensions escalate, then EU and US leaders could extend existing regimes, adding more individuals and companies onto banned lists. But if this is considered ineffective then more could be done to restrict Russia's access to capital markets and, possibly as a last resort, cutting Russia from international payments systems.

In the event of this, Russia would have to develop its own payments system, but this would create a liability for a Russian person or company complying with international sanctions and wanting access to Western markets.

"The sanctions in 2014 intended to make it difficult for Russian companies to get access to capital markets," Adams said. "The overall goal was to provide a powerful message after the annexation of Crimea so Ukraine and Russia could get to a common decision, but you could argue this has not happened."

Last month NATO general secretary Jens Stoltenberg said economic sanctions are preventing Russia from invading other countries, but since the Crimea invasion, Russia has been strongly accused of interfering in two separate election campaigns.

The new US Bill may be the first point at which the EU and US diverge on their approaches towards Russia, and will give those in Russia cause for encouragement. What happens next may define the approach for years to come.

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