

ISSUE BRIEF

# Secondary Sanctions' Implications and the Transatlantic Relationship

The Global Business & Economics Program (GBE) works to strengthen the already deep economic integration between Europe and the United States as well as promote transatlantic leadership in the global economy. GBE is committed to finding multilateral solutions to today's most pressing global economic opportunities and risks. Key challenges the program addresses include fostering broad-based economic growth, advancing understanding of the impact of economic sanctions, and defining the future shape of the rules-based international trade order.

UK Finance is the collective voice for the banking and finance industry. Representing more than 250 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation. We work for and on behalf of our members to promote a safe, transparent and innovative banking and finance industry. We offer research, policy expertise, thought leadership and advocacy in support of our work. We provide a single voice for a diverse and competitive industry. Our operational activity enhances members' own services in situations where collective industry action adds value.

SEPTEMBER 2019 SAMANTHA SULTOON & JUSTINE WALKER

## Economic Sanctions Initiative

*Economic sanctions have become a policy tool-of-choice for the US government. Yet sanctions and their potential pitfalls are often misunderstood. The Economic Sanctions Initiative (ESI) seeks to build a better understanding of the role sanctions can and cannot play in advancing policy objectives and of the impact of economic statecraft on the private sector, which bears many of the implementation costs.*

### Introduction

This paper has been jointly produced by the Atlantic Council's Economic Sanctions Initiative and UK Finance. The aim is to inform transatlantic dialogue with respect to cross-border legal, regulatory, and compliance considerations that may arise as a result of the imposition, or threatened imposition, of US secondary sanctions.

At the outset, two key points should be acknowledged. First, the risk appetite of commercial and financial institutions regarding where and how they operate is influenced by a range of factors, including regulatory and legal requirements of the jurisdictions, opportunities for growth, and market transparency, among many others. Decisions to engage in or withdraw from certain higher-risk markets due to potential sanctions scenarios may be made even where there is no legal obligation to do so. Second, each sovereign state has, within the scope of expected international norms, the right to choose and administer its own domestic and foreign policies. Where the implications of such decisions may be in contrast to the interests or views of key allies or partners, or raise conflicts of law considerations, thorough analysis should inform the policy decision.



On November 8th, 2018, Secretary of State Mike Pompeo and US Treasury Secretary Steven Mnuchin announce the reimposition of all US economic sanctions on Iran. *Source: US Department of State.*

Consequently, this paper seeks to help shape a broader transatlantic dialogue on the context of unilateral US secondary sanctions, the impact on the transatlantic relationship, and key considerations to support market stability, legal clarity, and compliance effectiveness.

## Context

The term secondary sanctions provokes strong reactions from allies and markets. This reaction is in spite of the fact that, to date, the actual imposition of secondary sanctions has been highly restrained. Nevertheless, the threat of and rhetoric around the United States' maximum pressure campaigns against Iran and North Korea, and escalating congressionally-mandated US sanctions targeting certain Russian oligarchs and key Russian defense companies, have resulted in additional non-US actors becoming exposed to a secondary sanctions risk. The notion that the United States may extend its jurisdiction beyond its territory and punish allies and foes alike for activities that were seemingly legal—and in some cases EU-government promoted—under the law of the land in which they were carried out has, in certain instances, left both private sector actors and European allies frustrated and alarmed. This

is particularly evident in the growing European political response to the threatened use of US secondary sanctions<sup>1</sup> in the contexts of Iran and Russia.

Due to the power of the US dollar, breadth of the US market, and dominance of the US financial system, even the threat of secondary sanctions prompts many non-US companies to change their behavior to avoid the risk of such sanctions. The potential of secondary sanctions has also prompted further de-risking as reputable multinational firms adjust their risk appetite and hedge against possible punitive action from Washington. Although this approach has furthered US policies, it has resulted in transatlantic political divergence and enhanced compliance uncertainty among private sector actors.

## Understanding Secondary Sanctions

When assessing the impacts of US secondary sanctions, it is first necessary to define the term. As there is some disagreement over the specific definition, for the purpose of this paper, US secondary sanctions, which are largely implemented and enforced by the US Treasury's Office of Foreign Assets Control (OFAC), are

<sup>1</sup> Ellie Geranmayeh and Manuel Lafont Rapnouil, *Meeting the challenge of secondary sanctions*, European Council of Foreign Relations, June 25, 2019, [https://www.ecfr.eu/publications/summary/meeting\\_the\\_challenge\\_of\\_secondary\\_sanctions](https://www.ecfr.eu/publications/summary/meeting_the_challenge_of_secondary_sanctions).

generally considered to be the threat of US sanctions against foreign individuals and entities for engaging in specified activities that may not have a US nexus.<sup>2</sup> US secondary sanctions effectively extend the United States' jurisdiction far beyond its borders and pressure US allies and adversaries to bend to US policies to varying degrees. While the Trump administration has repeatedly threatened secondary sanctions, the tool is more commonly introduced by the US Congress in legislation such as the Countering America's Adversaries Through Sanctions Act (CAATSA) of 2017,<sup>3</sup> the Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA) of 2010,<sup>4</sup> and the Hizballah International Financing Prevention Act of 2015,<sup>5</sup> among others, all of which were intended to strengthen or codify existing sanctions authorities. Through the use or threat of secondary sanctions, the United States is able to further discourage non-US actors from conducting business with designated entities, or even with a specified country—as is the intent with US sanctions on Iran and North Korea. In applying, or threatening to apply, secondary sanctions, the United States penalizes actors for engaging with sanctioned targets even without the jurisdiction to make that engagement illegal. In turn, secondary sanctions ratchet up pressure on the designated actor and magnify the impact of US unilateral actions on a regional and global scale. While the United States, or any independent country for that matter, is within its right to establish and implement its own domestic and foreign policies, including through excluding certain actors from its financial system, the reverberations from such policies extend far beyond its borders, and impact allies and foes alike.

There are some in the sanctions sphere who contend that secondary sanctions are merely an alternate form of OFAC sanctions enforcement. They argue that, through secondary sanctions, the United States is merely enforcing its own policy on the use of the

US dollar and access to the US financial system. Since OFAC enforcement actions can take years to come to fruition, secondary sanctions, as viewed through this lens, offer a far more expeditious tool than pursuing an enforcement action given how quickly they can be deployed.

### Primary versus Secondary Sanctions

Primary Sanctions prohibit transactions with a direct nexus to the administering country. For example, US primary sanctions are prohibitions—such as on trade, financial transactions, or other certain dealings—in which US persons may not engage absent authorization from OFAC exemption.<sup>6</sup> US persons in the OFAC context<sup>7</sup> include all US citizens and permanent resident aliens irrespective of where in the world they are located, all persons and entities within the United States, and all US incorporated entities and their foreign branches. In certain sanctions programs, foreign subsidiaries owned or controlled by US companies are also included.<sup>8</sup>

Secondary Sanctions are the threat of sanctions directed at third-country actors for engaging in certain activities with the targets of existing sanctions, regardless of a direct link to the administer-

ing country. For example, US secondary sanctions threaten to cut off non-US persons, such as European businesses, from the US financial system for transactions or certain other dealings with US-designated actors, such as designated Iranian or Russian businesses or sectors. The reach of the US dollar and US financial system provides for the reach of such secondary sanctions.

2 United States Department of the Treasury, "Basic Information of OFAC and Sanctions," Office of Foreign Assets Control, [https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq\\_all.html](https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq_all.html).

3 "Countering America's Adversaries Through Sanctions Act of 2017 (CAATSA)," Pub.L. 115-44, 84 Stat. 1114 (2017), [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/hr3364\\_pl115-44.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/hr3364_pl115-44.pdf).

4 "Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010," Pub.L. 111-195, 120 Stat. 1344 (2010), <https://www.treasury.gov/resource-center/sanctions/Documents/hr2194.pdf>.

5 "Hizballah International Financing Prevention Act of 2015," Pub.L. 114-102, 129 Stat. 2205 (2015), <https://www.congress.gov/bill/114th-congress/house-bill/2297/text>.

6 United States Department of the Treasury, "Basic Information on OFAC and Sanctions," Office of Foreign Assets Control, [https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq\\_all.html](https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq_all.html).

7 United States Department of the Treasury, "OFAC FAQs: General Questions," Office of Foreign Assets Control, February 6, 2019, [https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq\\_general.aspx#basic](https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_general.aspx#basic).

8 Ibid.

## Secondary Sanctions versus Material Support

Secondary sanctions, even when wielded as a threat, often prompt strong reactions from allies, particularly in Europe. The legal authority to impose primary US sanctions on foreign actors engaging in specified nefarious behavior, however, is common across most US sanctions programs and does not prompt the strong response from allies and partners that the use of secondary sanctions does. Rather than being defined broadly as secondary sanctions, however, this authority exists under the OFAC designation criterion of “material support.” From counterterrorism sanctions to the Global Magnitsky program, which targets those involved in serious human rights abuse or corruption,<sup>9</sup> the authority for the United States to sanction those providing material support, such as financial support or technology, to bad actors is prevalent. This authority is augmented by another designation criterion, which is also available under most sanctions programs, that allows OFAC to target those acting for or on behalf of a designated actor. OFAC’s ability to impose sanctions for such behaviors is delegated by the president to the Department of the Treasury and then to OFAC.

Curiously, use of the “material support” criterion for the application of sanctions is rarely questioned or criticized. Instead, there is a general recognition that this structure of targeting a designated actor’s network renders sanctions more effective. The United States and most likeminded governments support the notion of cutting off all means of financial, material, and technical support to designated actors, such as nuclear proliferators and terrorists. In fact, among allies, it is difficult to find coordinated criticism of this objective. Certain European Union (EU) sanctions programs, such as the recently introduced cyber sanctions,<sup>10</sup> include a similar criterion.

OFAC has used the “material support” designation criterion to target those providing assistance specifically in support of malign activities, such as terrorism or proliferation or human rights abuses, whereas secondary sanctions are generally viewed as broader and targeted towards arms-length commercial trans-

actions with a sanctions target. The broader, parallel secondary sanctions approach leaves compliance experts without a clear lens through which to scope their company’s operations and risk appetite. As a result, whether or not the secondary sanctions are actually used, the mere possibility that a company could be targeted for a commercial transaction yields caution. Whereas targeted or primary sanctions are intended to isolate an individual actor, secondary sanctions are intended to facilitate broader isolation of an entire market or country. When deployed against closed economies, such as North Korea, the impact on allies and partners is limited. As the United States expands the scope to target actors in open economies, such as Russia and China, without corresponding ally engagement and compliance clarification, frustration over the tool mounts. As long as OFAC remains the powerful and effective agency that it currently is, even the threat of secondary sanctions will continue to garner results. It is because of this outcome that secondary sanctions have become such an effective messaging and policy tool.

## Examples of Secondary Sanctions

Though references to and threats of secondary sanctions have increased exponentially during the Trump administration, the administration has acted with restraint in actually deploying the tool. Two fairly recent examples of secondary sanctions offer some insight into how the administration is implementing the tool.

### Iran

Following US President Donald J. Trump’s May 2018 announcement that the United States would withdraw from the Iran nuclear deal, or the JCPOA, the administration in November 2018 reimposed sanctions that targeted specific sectors of the Iranian economy, such as banking and finance, oil production and sales, and shipping, among others. At the time, the United States had an established system that mitigated some of the secondary sanctions concern among allies and partners regarding Iranian oil imports. This system included two key components. First, the Trump administration an-

9 United States Department of the Treasury, “Global Magnitsky Sanctions,” Office of Foreign Assets Control, <https://www.treasury.gov/resource-center/sanctions/Programs/pages/geomag.aspx>.

10 “Council Regulation (EU) 2019/796 of 17 May 2019 concerning restrictive measures against cyber-attacks threatening the Union or its Member States” (2019) *Official Journal of the European Union*, L1 129/1, <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L1.2019.129.01.0001.01.ENG&toc=OJ:L:2019:129:TOC>.



nounced certain 90- and 180-day wind-down periods, though those have since expired. Second, the Trump administration allotted a number of significant reduction exceptions, or SRE oil waivers, to “allow” certain countries to continue importing Iranian oil irrespective of the significant transactions involved.<sup>11</sup> The last eight SREs were withdrawn in May 2019 as the Trump administration strives to drive Iranian oil exports down to zero.<sup>12</sup>

In July 2019, the US State Department<sup>13</sup> announced secondary sanctions against China's Zhuhai Zhenrong Company Limited for engaging in a significant transaction involving Iranian crude oil, after the expiration of China's SRE in early May 2019. At the same time, OFAC listed Zhuhai Zhenrong and its CEO Youmin Li<sup>14</sup> as Specially Designated Nationals (SDNs) under the Iran sanctions<sup>15</sup> program. It remains to be seen if such actions were the beginning of a trend under the Iran sanctions program or an anomaly.

## Russia

In 2018, the Trump administration also imposed secondary sanctions<sup>16</sup> on a Chinese company and its director for engaging in significant transactions with third-country actors—this time with Russia. This sec-

ondary sanctions action was taken under Section 231 of CAATSA. In the action, the US imposed sanctions<sup>17</sup> on a Chinese entity, Equipment Development Department (EDD), and its director, Li Shangfu, for engaging in significant transactions with Russia's primary arms export entity, Rosoboronexport. EDD had purchased the Su-35 combat aircraft and S-400 surface-to-air missile system-related equipment from Russia.<sup>18</sup> CAATSA Section 231 mandates sanctions on any person who is determined to have knowingly engaged in a significant transaction with specified actors in Russia's defense and intelligence sectors.<sup>19</sup>

In contrast, the United States did not impose<sup>20</sup> such sanctions following Turkey's purchase of the same S-400<sup>21</sup> equipment—though the Trump administration did remove its NATO ally from the F-35 fighter jet program. This perceived inconsistency<sup>22</sup> is adding to both allies' and the compliance community's confusion regarding the application of the congressionally mandated sanctions.

11 David Mortlock and Nikki M. Cronin, *A Roadmap of the Re-Imposed Iran Sanctions*, Atlantic Council, November 2018, <https://www.atlantic-council.org/wp-content/uploads/2019/09/A-Road-Map-of-the-Re-Imposed-Sanctions.pdf>.

12 Ashish Kumar Sen, “A look at the implications of Trump's decision to end sanctions waivers for countries importing Iranian oil,” *New Atlanticist*, Atlantic Council, April 22, 2019, <https://www.atlanticcouncil.org/blogs/new-atlanticist/trump-ends-sanctions-waivers-for-countries-importing-iranian-oil/>.

13 United States Department of State, “The United States To Impose Sanctions on Chinese Firm Zhuhai Zhenrong Company Limited for Purchasing Oil From Iran,” US Department of State, July 22, 2019, <https://www.state.gov/the-united-states-to-impose-sanctions-on-chinese-firm-zhuhai-zhenrong-company-limited-for-purchasing-oil-from-iran/>.

14 United States Department of the Treasury “Iran-Related Designations,” Office of Foreign Assets Control, July 22, 2019, <https://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Pages/20190722.aspx>.

15 Exec. Order No. 13846 of August 6, 2018. “Reimposing Certain Sanctions With Respect to Iran,” 3 C.F.R. 1 (2018), [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/08062018\\_iran\\_eo.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/08062018_iran_eo.pdf).

16 Marshal Cohen and Nicole Gaouette, “US sanctions Chinese military for buying Russian weapons,” CNN Politics, September 21, 2018, <https://www.cnn.com/2018/09/20/politics/russia-china-sanctions-caatsa-state-dept/index.html>.

17 United States Department of State, “Sanctions Under Section 231 of the Countering America's Adversaries Through Sanctions Act of 2017 (CAATSA),” US Department of State, September 20, 2018, <https://www.state.gov/sanctions-under-section-231-of-the-countering-americas-adversaries-through-sanctions-act-of-2017-caatsa/>.

18 Lesley Wroughton and Patricia Zengerle, “U.S. sanctions China for buying Russian fighter jets, missiles,” Reuters, September 20, 2018, <https://www.reuters.com/article/us-usa-russia-sanctions/u-s-sanctions-china-for-buying-russian-fighter-jets-missiles-idUSKCNIM02TP>.

19 United States Department of State, “Sanctions Under Section 231 of the Countering America's Adversaries Through Sanctions Act of 2017 (CAATSA),” US Department of State, September 20, 2018, <https://www.state.gov/sanctions-under-section-231-of-the-countering-americas-adversaries-through-sanctions-act-of-2017-caatsa/>.

20 Patricia Zengerle, “U.S. lawmakers denounce Turkey's Russia arms purchase but unsure of next steps,” Reuters, July 25, 2019, <https://www.reuters.com/article/us-turkey-security-usa-congress/u-s-lawmakers-denounce-turkeys-russia-arms-purchase-but-unsure-of-next-steps-idUSKCN1UK2TF>.

21 Madeleine Jourg, “How President Trump Is Undercutting Pompeo in a Dispute Over Turkey's Purchase of a Russian Missile System,” *Time*, August 2, 2019, <https://time.com/5633196/trump-pompeo-turkey-sanctions-russia-s400/>.

22 Katie Bo Williams, Kevin Baron, and Marcus Weisgerber, “Graham: I Told Turkey They Can Avoid Sanctions If They Don't Activate Russian Radar,” *DefenseOne*, July 25, 2019, <https://www.defenseone.com/politics/2019/07/graham-trump-asked-me-call-turkey-s-400-deal/158706/>.



A S-400 surface-to-air-missile system (SAM) takes part in a rehearsal for Russia's 2009 Victory Day parade in Moscow.  
Source: Vitaly V. Kuzmin.

## Compliance Challenges for Non-US Actors: Key Russia Sanctions Takeaways

Secondary sanctions actions, risk of exposure to activity that may be subject to secondary sanctions, and the increasing US rhetoric around the tool have prompted companies in Europe and beyond to take the threat of secondary sanctions seriously. More broadly, recent OFAC enforcement actions and Trump administration messaging that further enforcement is forthcoming have prompted European and other companies to re-focus their risk management approaches on where and how business operates.

The uncertainty surrounding the application of secondary sanctions has increased their impact<sup>23</sup> and also created considerable cross-border political, compli-

ance, and legal discord. For instance, while the United States and the EU have several shared foreign policy concerns, including those stemming from Russia's 2014 military incursion in Ukraine, notable transatlantic differences of approach have emerged in recent years. The 2017 CAATSA legislation, which imposes sanctions on Iran, Russia, and North Korea, created a recent fissure point. Within CAATSA<sup>24</sup> specifically, there are mandatory secondary sanctions on a foreign entity that the president determines facilitates "significant transactions" with sanctioned actors. The lack of clear guidance<sup>25</sup> around this term has exacerbated the discord.

Following the July 2018 summit between Trump and Russian President Vladimir Putin in Helsinki,<sup>26</sup> and the

23 Ellie Geranmayeh and Manuel Lafont Rapnouil, *Meeting the challenge of secondary sanctions*, European Council of Foreign Relations, June 25, 2019, [https://www.ecfr.eu/publications/summary/meeting\\_the\\_challenge\\_of\\_secondary\\_sanctions](https://www.ecfr.eu/publications/summary/meeting_the_challenge_of_secondary_sanctions).

24 "Countering America's Adversaries Through Sanctions Act of 2017 (CAATSA)," Pub.L. 115-44, 84 Stat. 1114 (2017), [https://www.treasury.gov/resource-center/sanctions/Programs/Documents/hr3364\\_pl115-44.pdf](https://www.treasury.gov/resource-center/sanctions/Programs/Documents/hr3364_pl115-44.pdf).

25 United States Department of the Treasury, "OFAC FAQs: Other Sanctions Programs," Question 545, Office of Foreign Asset Control, September 6, 2019, [https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq\\_other.aspx#sec\\_228](https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_other.aspx#sec_228).

26 Ron Elving, "Trump's Helsinki Bow To Putin Leaves World Wondering: Why?" NPR, July 17, 2018, <https://www.npr.org/2018/07/17/629601233/trumps-helsinki-bow-to-putin-leaves-world-wondering-whats-up.s>

subsequent passage of CAATSA, the US Congress has increasingly sought ways to increase its influence and control over US foreign policy towards Russia. This interest has resulted in the drafting of a number of additional bills that would extend provisions set out in CAATSA.

Prompted in part by CAATSA and pending US legislation, there has been a rise in Russia-related financing denominated in currencies other than US dollars. In short, the lack of US lender involvement and US dollar nexus has resulted in the industry reporting a growing set of transactions that do not include a direct US relationship and, therefore, are out of the scope of primary sanctions. These trends have, in part, influenced both the US Congress and the Trump administration's appetite for secondary sanctions. However, US government sanctions implementation infrastructure is not yet able to address the vulnerabilities and challenges for third-country actors seeking to comply with US primary and secondary sanctions, such as through licensing and guidance. Instead, a few key trends have developed around the scope and application of US secondary sanctions that warrant closer analysis and thoughtful consideration by policymakers considering employing US secondary sanctions.

### Trend #1: Complications for Non-US Actors in Exiting Relationships to Avoid Secondary Sanctions

*Context:* Financial institutions and other private companies, when entering into a permissible transaction, will often rely on contractual provisions to allow space for potential future sanctions activity and according compliance. These contractual provisions are generally comprised of representations and undertakings that the borrower makes to lenders. For instance, should the borrower breach the statements or become a sanctioned actor, lenders are generally empowered to exit the transaction or relationship. These clauses rely on primary sanctions, however, and in a secondary sanctions scenario (i.e., where the activity is not actually prohibited) this can render such clauses ineffective in mooted the contract and the actor is unable to invoke force majeure. This leaves a lender unable

to take advantage of a US authorized wind-down period, for example, to unwind existing relationships with newly sanctioned actors. To illustrate this further we highlight the following case study scenario.

*Specific Scenario:* A European lender enters into a project finance transaction denominated in euros. At the time of entering into the contract there are no US or EU sanctions in place that would impact contractual activity. Subsequent to entering into the agreement, the United States threatens to impose sanctions upon persons involved in the project, but not to target the project itself. In a primary sanctions context, the lender would normally seek to trigger illegality based on the aforementioned contractual provisions; however, in this instance a European lender would have no legal basis to do so because there is no legal prohibition through which to trigger the aforementioned contractual provisions. Equally, the European lender cannot rely upon an undertaking that the borrower would prompt and cause the lender to be in breach of sanctions because, in this case, there are no sanctions being breached. This is just the new threat of sanctions being imposed due to association with a specific project for which no sanctions issues existed when the contract was signed at the project's inception. In this scenario, a European bank with a US presence or US correspondent relationship could be scrutinized by US authorities and, while wishing to comply with US sanctions, may have no immediate contractual ability to unwind its position and, therefore, face the threat of such US sanctions.

### Trend #2: The Undefined Scope of "Significant Transaction"

*Context:* The use of the term "significant transaction" is increasingly being incorporated across a range of existing and draft US legislation. The term is already used at least a handful of times across CAATSA without ever being clearly defined. This opacity creates significant compliance challenges for non-US actors seeking to comply with US sanctions. For example, Section 228<sup>27</sup> of CAATSA mandates secondary sanctions (with limited exceptions) on non-US persons for knowingly facilitating "significant transactions" for or on behalf of certain persons sanctioned pursuant to Ukraine-/

---

27 Ambassador Daniel Fried and Brian O'Toole, *The New Russia Sanctions Law—What it does and How to Make It Work*, Atlantic Council, September 2017, [https://www.atlanticcouncil.org/images/The\\_New\\_Russia\\_Sanctions\\_Law\\_web\\_0929.pdf](https://www.atlanticcouncil.org/images/The_New_Russia_Sanctions_Law_web_0929.pdf).



Russia-related sanctions authorities. Helpfully, OFAC provided guidance<sup>28</sup> on the application of “significant transactions” in Section 228 of CAATSA, listing certain factors that it will consider when making the determination on whether or not a transaction is significant. Likewise, the State Department has also set out various aspects it will draw upon to determine whether an investment is significant pursuant to Section 225 of CAATSA, which mandates sanctions on foreign persons making significant investments in special Russian crude oil projects.<sup>29</sup> While the provision of such information is useful, unfortunately the list in both cases is non-exhaustive and stresses a case-by-case approach, hampering non-US private sector actors’ ability to gauge the risk of the imposition of sanctions. The guidance and caveats illustrate that the United States maintains leeway in assessing whether a transaction or investment will qualify as significant.

*Specific Scenario:* The implications of this leeway raised immediate compliance uncertainties following the April 2018 designations<sup>30</sup> of Russian oligarchs and their businesses pursuant to CAATSA. For allies and partners, particularly in Europe, these designations highlighted three key disadvantages for non-US persons seeking to avoid running afoul of US sanctions:

- **Lack of a mechanism for a non-US person to secure formal clarity that a transaction or activity is permissible.** While the April 2018 designations were limited to a group of specified individuals and entities, the actual impact was considerably broader due to ownership and control factors on entities in Europe and elsewhere. Such exposure created a plethora of uncertainties on how to manage relationships among a wide net of internationally located entities. At the practical level, it also raised a long list of queries on how to deal with payments such as local salaries, processing of domestic pension commitments, tax payments to non-US government authorities, local government council charges, utility bill payments, and so forth.

- **Inability to seek authorization for certain activities.** With no formal US nexus, non-US persons have limited, if any, ability to apply to OFAC for a license to engage in activity that would otherwise be prohibited.<sup>31</sup> This is the case even when the activity may be consistent with US foreign policy interests, which is often a key consideration for the issuance of a license.
- **Limited outreach to non-US actors seeking to respect US sanctions.** The US government, and OFAC, in particular, often engages in helpful, targeted outreach when new sanctions regimes or key changes occur to support the US private sector’s understanding of and compliance with the sanctions. However, since OFAC administers and enforces US sanctions, such outreach is often—though fortunately not always—limited to US institutions. Since non-US companies are often directly exposed to the threat of US sanctions—in some cases, such as through aspects of the April 2018 CAATSA actions, more so than US institutions—they are disadvantaged by not having regular access to such outreach events and opportunities to engage with OFAC regarding technical aspects of the sanctions programs.

In sum, the April 2018 CAATSA sanctions illustrated myriad challenges faced by affected operators outside the United States, particularly in allied countries. This is particularly so given US secondary sanctions often increase the complexity of compliance programs for global companies and banks, and the lack of guidance for and engagement with non-US actors increases the likelihood of an inadvertent breach of sanctions.

### Trend #3: The Undefined Application of “Significant Transaction”—Legal Fees and Court Awards for Non-US Persons

*Context:* Persons subject to US sanctions can be and are subject to ongoing civil and criminal action outside US jurisdiction, which can also give rise to US secondary sanctions considerations as legal fees and court judgments issued outside the United States need to be

28 United States Department of the Treasury, “OFAC FAQs: Other Sanctions Programs,” Section 228, Office of Foreign Asset Control, September 6, 2019, [https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq\\_other.aspx#sec\\_228](https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_other.aspx#sec_228).

29 Fried and O’Toole, *The New Russia Sanctions Law*.

30 United States Department of the Treasury, “Treasury Designates Russian Oligarchs, Officials, and Entities in Response to Worldwide Malign Activity,” US Treasury, April 6, 2018, <https://home.treasury.gov/news/press-releases/sm0338>.

31 United States Department of the Treasury, “OFAC FAQs: General Questions,” Office of Foreign Assets Control, February 6, 2019, [https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq\\_general.aspx#basic](https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_general.aspx#basic).





The oil tanker HUGO from the National Iranian Tanker Company arrives in the port of Rotterdam, Netherlands, in February 2017. *Source: Kees Torn.*

paid. In the majority of OFAC sanctions programs,<sup>32</sup> a general license authorizes the provision of legal services and the processing of associated payments. Such authorizations, however, do not extend to non-US persons or beyond US jurisdiction leaving EU and other financial institutions in a legal bind.

*Specific Scenario—Court Fees:* A non-US financial institution is asked to process transactions connected to a non-US court action. One of the parties involved in the transaction is subject to US secondary sanctions. Beyond the designation there is no US nexus and the transaction is not in US dollars. The key challenge for the non-US financial institution is determining whether processing the court-related transactions could be considered a significant transaction and expose the financial institution to the risk of secondary sanctions. As mentioned above, there is no precise definition of a significant transaction. While OFAC guidance indicates that the agency will generally consider the totality of the facts and circumstances when determining whether transactions are significant, the agency maintains discretion to consider such other factors that the secretary of the Treasury deems relevant on a case-by-case basis.<sup>33</sup> Without clear guidance or the ability to obtain such guidance from OFAC, the financial insti-

tution is left with legal uncertainty as it contemplates processing a court-related transaction.

*Specific Scenario—Legal Fees:* A non-US financial institution is asked to process the receipt of legal fees for its law firm client who is acting on behalf of persons subject to US sanctions with a potential secondary sanctions nexus. Depending on the nature of the court action, such transactions can be sizable and involve a number of transactions that, if the court action takes several months or years, can be frequent in nature. Where an OFAC SDN is successful in defending or as a claimant in a non-US court action, this can result in an award being made to the OFAC SDN for court cost and/or an award for a successful claim. Such a transaction can be sizable. Where an award is made against an OFAC SDN—given that this will result in the person being deprived of funds—it would not have a detrimental impact on the policy objectives of the sanctions program. However, there is the possibility that the SDN will appeal. An appeal can result in a requirement for the OFAC SDN to place funds with the court to demonstrate that the SDN has the means to pay the award in the event that appeal is unsuccessful, and if the SDN is successful there would be a need to send the funds back to the OFAC SDN.

32 See 31 CFR § 515.512 as an example of such an authorization in the Cuba sanctions program. While the payment of court fees and legal fees and the processing of such fees by financial institutions is often authorized by OFAC across sanctions program, the agency has also issued legal guidance. However, the authorizations and guidance do not apply to non-US persons.

33 See, for example, 31 CFR § 561.404 and OFAC FAQ: Iran Sanctions, FAQ # 554.

Access to justice is a basic principle of international law. However, secondary sanctions can impact the ability of OFAC SDNs to have access to justice outside of the United States and also restrict non-OFAC SDNs' ability to comply with court orders issued outside the United States due to financial institutions' reluctance to process transactions. While there is some guidance indicating that a transaction is not significant if US persons would not require an OFAC-specific license to participate in it (see OFAC FAQs<sup>34</sup> 542, 545, and 574), this is not clear across programs.

### Key Considerations and Policy Recommendations

As both the US Congress and the Trump administration have become increasingly willing to use the threat of secondary sanctions, in addition to the increasing application of unilateral sanctions, the following lessons should be considered before wielding such tools:

- Proactively mitigate the unintended consequences.** Secondary sanctions should not be applied without viable tools to mitigate the unintended impact where needed. A wind-down period should be standard practice to allow time for disentanglement. Waivers, such as the Iran oil SREs or the ongoing electricity waiver<sup>35</sup> to allow Iraq to continue obtaining electricity from Iran, should be included and available for use. This means that the executive branch must have the political appetite and ability to employ them if appropriate, and not merely reference them—as in the case of the national security waivers administered by the State Department under Section 236 of CAATSA.
- Use sanctions in support of a cogent objective.** When applying sanctions, primary or secondary, they must be used in support of a clearly defined and well-informed policy objective. Such an objective is far more likely to be realized if the sanctions are developed multilaterally. If the policy goal is to isolate an economy, that should be fully considered, including the implications for allies. Threatening secondary sanctions on Venezuela,<sup>36</sup> for example, while
- also trying to gain support of likeminded countries may not be the most effective way forward. Instead, focusing on clear, coordinated action is certain to be more effective and the pathway to easing sanctions far clearer.
- Default to primary, not secondary, sanctions.** Primary sanctions are clearer. There is a reason that the United States generally defaults to primary sanctions, even when targeting such adversarial actors as Iran's Islamic Revolutionary Guard Corps. The messaging is far more transparent, and the implementation and compliance far simpler.
- Support compliance.** The United States could help the private sector better understand and effectively adhere to secondary sanctions by developing clear guidance for non-US persons impacted by US sanctions—or the threat of US secondary sanctions. As it currently stands, without a clear nexus to the United States, there is little opportunity to obtain guidance from OFAC on the scope or application of US secondary sanctions. Non-US companies that are striving to do the right thing are unable to obtain clear answers. Further, those companies are generally not eligible to apply to OFAC for specific licenses even where the proposed activity may otherwise align with US policy objectives. In addition to guidance, OFAC could support non-US actor compliance by raising awareness of its existing compliance resources (hotline, online FAQs, annual symposium, etc.) and increasing its international outreach and accessibility with the private sector. As it stands, the non-US private sector is left to hedge against potential US sanctions and this is having broader negative impacts on alliances, market risk appetite, and long-term US economic and financial hegemony.
- Provide clarity for non-US actors on the application of general licenses and definition of “significant transaction.”** OFAC could provide clarity (and some comfort) to non-US actors seeking to comply with US sanctions by issuing further guidance on the application of OFAC general licenses to non-US persons. While OFAC's jurisdiction does not extend

34 United States Department of the Treasury, “Basic Information on OFAC and Sanctions,” Office of Foreign Assets Control, [https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq\\_all.html](https://www.treasury.gov/resource-center/faqs/Sanctions/Documents/faq_all.html).

35 John Davison, Ahmed Rasheed, and Valerie Volcovici, “U.S. allows Iraq to import Iranian energy for three more months,” Reuters, June 15, 2019, <https://www.reuters.com/article/us-usa-iran-iraq/u-s-allows-iraq-to-import-iranian-energy-for-three-more-months-idUSKCN1TG08X>.

36 Samantha Sultoon, *Spotlight: Next Steps with Venezuela*, Atlantic Council, April 25, 2019, <https://www.atlanticcouncil.org/blogs/new-atlanticist/spotlight-next-steps-with-venezuela>.

beyond US persons, those within the United States, and all US-incorporated entities and their foreign branches (and in certain programs foreign subsidiaries owned or controlled by US companies),<sup>37</sup> many non-US actors are exposed to secondary sanctions risk through their international footprint. Such guidance could clarify for these non-US actors the US government's expectations as it pertains to wind downs, humanitarian transactions, and other sanctions-related transactions on which non-US persons currently have limited clarity or assistance. Guidance also needs to be clearer on the definition and application of a "significant transaction." In addition to published guidance, OFAC could further promote the use of its existing compliance resources for non-US actors seeking clarification on the management of secondary sanctions exposure.

- **Conduct advance due diligence across markets and alliances.** As the US Congress contemplates new sanctions legislation with implications for allies and partners, a thorough assessment of the potential implications of such legislation should be conducted in advance of moving the legislation forward. Engagement with allies and partners as to the potential risks to their economies and knock-on impacts to the global supply chain should be standard practice. While the United States and the EU may differ on their perspectives of the sanctions on aluminum giant Rusal,<sup>38</sup> the United States was unprepared to mitigate the unintended consequences<sup>39</sup> of its actions, and the US Congress was unnecessarily surprised by the impact of its legislation on an alliance it purports to support. Had thorough advance

due diligence been conducted, OFAC would have been poised to more effectively and proactively address the situation and the US Congress could have considered revising the legislation to calibrate the impact on allies.

- **Recognize the implications of secondary sanctions.** US policymakers need to recognize that wielding blunt tools, like secondary sanctions, can alienate key allies and prompt them to pursue seemingly adversarial actions. For example, following the US withdrawal from the JCPOA, the E3 (the United Kingdom, Germany, and France) announced the creation of the special purpose vehicle (SPV)<sup>40</sup> to facilitate Iran-related trade. While the SPV is currently limited to transactions that are consistent with US sanctions,<sup>41</sup> the notion that US policies would drive allies to develop alternate payment systems to exclude the United States should set off alarm bells in Washington. Similarly, the Trump administration's decision to allow lawsuits against foreign entities "trafficking" in US confiscated property under Title III of the Helms-Burton Law<sup>42</sup> is also prompting action from key allies.<sup>43</sup> Both the EU and Canada are considering options at the World Trade Organization. The EU is also reviewing its blocking statute that allows EU companies sued in the United States to recover any damages from US claimants in EU courts. As former US Treasury Secretary Jack Lew said<sup>44</sup> at the Atlantic Council in Washington in February 2019, allies and adversaries are testing the United States' financial plumbing. Washington needs to be mindful of the impact of its policy decisions. Such decisions should not be prompting key

37 United States Department of the Treasury, "OFAC FAQs: General Questions," Office of Foreign Assets Control, February 6, 2019, [https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq\\_general.aspx#basic](https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_general.aspx#basic).

38 United States Department of the Treasury, "Treasury Designates Russian Oligarchs, Officials, and Entities in Response to Worldwide Malign Activity," US Treasury, April 6, 2018, <https://home.treasury.gov/news/press-releases/sm0338>.

39 Alanna Petroff, "Sanctions have sent aluminum soaring. That could hurt your wallet," CNN Business, April 11, 2018, <https://money.cnn.com/2018/04/11/investing/aluminum-prices-sanctions-rusal/index.html>.

40 Samantha Sultoon, "Europe Unlikely to Avoid Trump's Iran Sanctions," *New Atlanticist*, Atlantic Council, September 25, 2018, <https://www.atlanticcouncil.org/blogs/new-atlanticist/europe-unlikely-to-avoid-trump-s-iran-sanctions>.

41 Brian O'Toole, "Facing Reality: Europe's Special Purpose Vehicle Will Not Challenge US Sanctions," Atlantic Council, January 31, 2019, <https://www.atlanticcouncil.org/blogs/iransource/facing-reality-europe-s-special-purpose-vehicle-will-not-challenge-us-sanctions>.

42 Samantha Sultoon, "Trump pursuing the right goals in Cuba, but in the wrong way," *Las Vegas Sun*, April 27, 2019, <https://lasvegassun.com/news/2019/apr/27/trump-pursuing-the-right-goals-in-cuba-but-in-the/>.

43 "Joint Statement by Federica Mogherini, Chrystia Freeland, and Cecilia Malmström on the decision of the United States to further activate Title III of the Helms Burton (Libertad) Act," April 17, 2019, [https://eeas.europa.eu/headquarters/headquarters-homepage/61181/joint-statement-federica-mogherini-chrystia-freeland-and-cecilia-malmstrom-C3%B6m-decision-united\\_en](https://eeas.europa.eu/headquarters/headquarters-homepage/61181/joint-statement-federica-mogherini-chrystia-freeland-and-cecilia-malmstrom-C3%B6m-decision-united_en).

44 David A. Wemer, "Buy-In From Allies Critical for Effective Sanctions, Says Former US Treasury Secretary Lew," *New Atlanticist*, Atlantic Council, February 19, 2019, <https://www.atlanticcouncil.org/blogs/new-atlanticist/buy-in-from-allies-critical-for-effective-sanctions-says-former-us-treasury-secretary-lew>.

allies to consider or pursue countermeasures.<sup>45</sup> The impact of US policies should also not be encouraging allies and adversaries to avoid using US dollars nor should it prompt the longer-term development of payment systems and structures that intentionally exclude the United States.

## Conclusion

Recent cases of US sanctions have demonstrated that, as currently structured, the US licensing framework, FAQs, and related enforcement information while comprehensive in scope do not provide sufficient clarity for non-US companies seeking to adhere to the US sanctions. This is compounded by the escalating threat of secondary sanctions against European and other non-US companies. US secondary sanctions may compel non-US companies to comply with US sanctions policy, but the cost to the transatlantic relationship, compliance implementation, and market stability for non-US actors should not be underestimated.

**Samantha Sultoon** is a visiting senior fellow with the Atlantic Council's Global Business & Economics Program and the Scowcroft Center for Strategy and Security. Samantha is also an international affairs fellow with the Council on Foreign Relations. Formerly, she served as a sanctions policy expert for the Department of the Treasury's Office of Foreign Assets Control (OFAC). Prior to her work at OFAC, Samantha was an intelligence advisor in the Treasury Department's Office of Intelligence and Analysis and a risk expert for the World Bank.

**Dr Justine Walker** has overall responsibility for the UK Finance programme on international sanctions compliance. Regarded as a global specialist in economic sanctions she has acted as a national expert on the financing of weapons of mass destruction (WMD) matters, sits on numerous international financial sanctions expert groups and is chair of the European Banking Federation's group on financial sanctions. She has extensive experience of working with foreign governments, international bodies and financial institutions and has contributed to numerous publications on counter proliferation financing and the management of high risk sanctions scenarios. Justine holds a PhD from the University of St Andrews.

---

45 Ellie Geranmayeh and Manuel Lafont Rapnouil, *Meeting the challenge of secondary sanctions*, European Council of Foreign Relations, June 25, 2019, [https://www.ecfr.eu/publications/summary/meeting\\_the\\_challenge\\_of\\_secondary\\_sanctions](https://www.ecfr.eu/publications/summary/meeting_the_challenge_of_secondary_sanctions).



This issue brief is part of the Atlantic Council's Economic Sanctions Initiative and is made possible by generous support through Navigant Consulting, Inc., PricewaterhouseCoopers, Procter & Gamble, and the Hon. David D. Aufhauser.

This issue brief is written and published in accordance with the Atlantic Council Policy on Intellectual Independence. The authors are solely responsible for its analysis and recommendations. The Atlantic Council and its donors do not determine, nor do they necessarily endorse or advocate for, any of this issue brief's conclusions.



## UK FINANCE

This report is intended to provide general information only and is not intended to be comprehensive or to provide legal, regulatory, financial or other advice to any person. Information contained in this report based on public sources has been assumed to be reliable and no representation or undertaking is made or given as to the accuracy, completeness or reliability of this report or the information or views contained in this report. None of UK Finance or any of their respective members, officers, employees or agents shall have any liability to any person arising from or in connection with any use of this report or any information or views contained in this report. © 2019, UK Finance.



### CHAIRMAN

\*John F.W. Rogers  
\*John F.W. Rogers

### EXECUTIVE CHAIRMAN EMERITUS

\*James L. Jones

### CHAIRMAN EMERITUS

Brent Scowcroft

### PRESIDENT AND CEO

\*Frederick Kempe

### EXECUTIVE VICE CHAIRS

\*Adrienne Arsht  
\*Stephen J. Hadley

### VICE CHAIRS

\*Robert J. Abernethy  
\*Richard W. Edelman  
\*C. Boyden Gray  
\*Alexander V. Mirtchev  
\*Virginia A. Mulberger  
\*W. DeVier Pierson  
\*John J. Studzinski

### TREASURER

\*George Lund

### SECRETARY

\*Walter B. Slocombe

### DIRECTORS

Stéphane Abrial  
Odeh Aburdene  
Todd Achilles  
\*Peter Ackerman  
Timothy D. Adams  
Bertrand-Marc Allen  
\*Michael Andersson  
David D. Aufhauser  
Colleen Bell  
Matthew C. Bernstein  
\*Rafic A. Bizri  
Dennis C. Blair  
Philip M. Breedlove  
Reuben E. Brigety II  
Myron Brilliant  
\*Esther Brimmer  
R. Nicholas Burns  
\*Richard R. Burt  
Michael Calvey  
James E. Cartwright  
John E. Chapoton  
Ahmed Charai  
Melanie Chen  
Michael Chertoff  
\*George Chopivsky  
Wesley K. Clark  
\*Helima Croft  
Ralph D. Crosby, Jr.  
Nelson W. Cunningham  
Ivo H. Daalder  
\*Ankit N. Desai  
\*Paula J. Dobriansky  
Thomas J. Egan, Jr.  
\*Stuart E. Eizenstat  
Thomas R. Eldridge  
\*Alan H. Fleischmann  
Jendayi E. Frazer  
Ronald M. Freeman  
Courtney Geduldig  
Robert S. Gelbard  
Gianni Di Giovanni  
Thomas H. Glocer  
John B. Goodman  
\*Sherri W. Goodman  
Murathan Günal  
\*Amir A. Handjani  
Katie Harbath  
John D. Harris, II  
Frank Haun  
Michael V. Hayden  
Brian C. McK. Henderson  
Annette Heuser  
Amos Hochstein  
\*Karl V. Hopkins  
Robert D. Hormats  
Andrew Hove  
\*Mary L. Howell  
Ian Ihnatowycz  
Wolfgang F. Ischinger  
Deborah Lee James  
Reuben Jeffery, III  
Joia M. Johnson  
Stephen R. Kappes

\*Maria Pica Karp  
Andre Kelleners  
Sean Kevelighan  
Henry A. Kissinger  
\*C. Jeffrey Knittel  
Franklin D. Kramer  
Laura Lane  
Richard L. Lawson  
Jan M. Lodal  
Douglas Lute  
Jane Holl Lute  
William J. Lynn  
Wendy W. Makins  
Mian M. Mansha  
Chris Marlin  
Gerardo Mato  
Timothy McBride  
John M. McHugh  
H.R. McMaster  
Eric D.K. Melby  
Franklin C. Miller  
\*Judith A. Miller  
Susan Molinari  
Michael J. Morell  
Richard Morningstar  
Mary Claire Murphy  
Edward J. Newberry  
Thomas R. Nides  
Franco Nuschese  
Joseph S. Nye  
Hilda Ochoa-Brillembourg  
Ahmet M. Oren  
Sally A. Painter  
\*Ana I. Palacio  
Kostas Pantazopoulos  
Carlos Pascual  
Alan Pellegrini  
David H. Petraeus  
Thomas R. Pickering  
Daniel B. Poneman  
Dina H. Powell  
Robert Rangel  
Thomas J. Ridge  
Michael J. Rogers  
Charles O. Rossotti  
Harry Sachinis

Rajiv Shah  
Stephen Shapiro  
Wendy Sherman  
Kris Singh  
Christopher Smith  
James G. Stavridis  
Richard J.A. Steele  
Paula Stern  
Robert J. Stevens  
Mary Streett  
Nathan D. Tibbits  
Frances M. Townsend  
Clyde C. Tuggle  
Melanne Verveer  
Charles F. Wald  
Michael F. Walsh  
Ronald Weiser  
Geir Westgaard  
Olin Wethington  
Maciej Witucki  
Neal S. Wolin  
Jenny Wood  
Guang Yang  
Mary C. Yates  
Dov S. Zakheim

### HONORARY DIRECTORS

James A. Baker, III  
Ashton B. Carter  
Robert M. Gates  
Michael G. Mullen  
Leon E. Panetta  
William J. Perry  
Colin L. Powell  
Condoleezza Rice  
George P. Shultz  
Horst Teltschik  
John W. Warner  
William H. Webster

*\*Executive Committee Members  
List as of September 11, 2019*



The Atlantic Council is a nonpartisan organization that promotes constructive US leadership and engagement in international affairs based on the central role of the Atlantic community in meeting today's global challenges.

© 2019 The Atlantic Council of the United States. All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means without permission in writing from the Atlantic Council, except in the case of brief quotations in news articles, critical articles, or reviews. Please direct inquiries to:

Atlantic Council

1030 15th Street, NW, 12th Floor,  
Washington, DC 20005

(202) 463-7226, [www.AtlanticCouncil.org](http://www.AtlanticCouncil.org)