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Sanctions Compliance Best Practices

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Sanctions Compliance: Who Must Comply and Why?

- Russian subsidiaries are not US/EU persons (i.e., there is no formal requirement to comply with US/EU sanctions)
- Sanctions compliance risks arise when there is a US/EU jurisdictional nexus:
 - Managers that are US/EU persons are involved in a particular transactions
 - US/EU companies are involved in a particular transaction
 - US/EU IT-platforms are used for the purposes of particular activities
 - USD payments are carried out in the course of particular transactions
 - *US export control*: US-originating controlled goods or non-US made goods incorporating more than 25% of controlled US content (more than 10% - for military items) are supplied under a particular transaction ("*De Minimis*" rule)
- Sanctions compliance risks arise when a subsidiary is required to comply with sanctions by virtue of its corporate policy

Sanctions Compliance: US Secondary Sanctions

- In the absence of the US jurisdictional nexus there is a risk of imposition of US secondary sanctions:
 - For operating in Crimea (Executive Order 13685)
 - Pursuant to CAATSA:
 - *Section 228*: for facilitating significant transactions for or on behalf of persons "subject to sanctions imposed by the US" with respect to Russia
 - *Section 226 (relevant for financial institutions only)*: for engaging in significant transactions involving certain defense- and energy-related activities or knowingly facilitating significant financial transactions on behalf of any Russian SDNs designated under Ukraine-related sanctions program
 - CAATSA provides for a large number of grounds (e.g., investment in or facilitation of privatization of state-owned assets, development of energy export pipelines, investment in special Russian crude oil projects, transfer of arms and related materiel to Syria, activities undermining cybersecurity, etc.)

Sanctions Compliance: Contractual Mechanisms

- Force majeure clause: will this work?
- Sanctions compliance clause:
 - May work if compliance with the US/EU sanctions is mutually agreed by the parties, but:
 - Russian supervising authorities and courts do not recognize the US/EU sanctions imposed against Russia as such
 - Should a dispute arise, Russian courts may potentially disregard sanctions compliance clauses as being contrary to Russian public policy - *Siemens case*
- In order to avoid a situation where Russian public policy-based arguments may be invoked by the counterparty (if a dispute arise):
 - include broad trade compliance clauses without making direct references to US/EU sanctions
 - include export control compliance provisions (Russia is a party to the Wassenaar Arrangement)

Sanctions Compliance: Additional Mechanisms

- Be precise when providing description of goods/services to be supplied/provided (where applicable)
- Demand end-user certificate (where applicable)
- Choose foreign governing law and dispute resolution venue outside Russia (where applicable)
- Consider developing a business model where goods would be supplied directly from foreign entities that are bound by the sanctions of their respective jurisdictions, where Russian subsidiaries perform just marketing functions

Implementation of Sanctions Compliance Policies

- US authorities (OFAC) require that sanctions compliance programs/policies must be implemented by:
 - US companies
 - US and non-US subsidiaries of US companies
 - All legal entities that are engaged in business with US companies
- When deciding on sanctions enforcement action, US authorities consider absence of sanctions compliance programs/policies as an aggravating factor
- To mitigate sanctions compliance risks in this regard consider the following:
 - developing and implementing sanctions compliance programs/policies
 - requiring the distributors/dealers to have sanctions compliance programs/policies in place
 - performing proper due diligence of counterparties from the sanctions and export control perspectives (i.e., screening)
 - monitoring developments in the sanctions legislation (especially US secondary sanctions, as well as their implementation practice)
 - screening of the counterparties as part of KYC and intake procedures

Sanctions screening techniques

- In order to screen your Russian counterparties we recommend the following screening tools:
 - Russian State Register of Legal Entities (“EGRUL”) of the Federal Tax Service provides information on all legal entities (<https://service.nalog.ru/vyp/>) - information on all Russian legal entities, ownership structure and general managers
 - “Spark” database (<http://www.spark-interfax.ru/Front/Index.aspx>, www.e-disclosure.ru) – most comprehensive search tool, provides information available in the EGRUL, as well as other publicly disclosed data
 - Corporate documents that companies must disclose
 - Corporate websites (both of the target and of its affiliates)
 - Open sources (mass media publications)
- In all unclear cases request your Russian counterparty in writing to disclose the ownership structure and ultimate beneficiaries, or to make a formal negative representation

Russian initiatives on counter sanctions

What is next?



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Thank you!

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