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Sectoral sanctions in the UK post-Brexit

*In 2014, the European Union adopted a package of restrictive measures targeting sectorial cooperation and exchanges with the Russian Federation. These controls focus on certain sectors of the Russian economy, initially those specifically linked to Russia's involvement in Eastern Ukraine (the "**Sectoral Sanctions**"). If the UK leaves the EU with no deal in place, the scope of the Sectoral Sanctions will encompass certain UK entities connected to the 11 in-scope Russian entities. This may have consequences for both these UK connected entities and for any EU bodies and individuals who do, or wish to do, business with them.*

BACKGROUND TO THE SECTORAL SANCTIONS

In general terms, although not banning investments or freezing assets, sectoral sanctions apply to specific transactions and entities in a given sector. The EU adopted the measures contained in the Sectoral Sanctions for a number of reasons, although one of the primary purposes was to limit the access of Russian State-owned financial institutions (and their non-EU majority-owned subsidiaries) to EU capital markets.

The Sectoral Sanctions were widened on a number of occasions in 2014 and 2015, with the following eleven entities now specifically identified: Gazprombank; Gazprom Neft; OJSC Oboronprom; Rosselkhozbank; Rosneft; Sberbank; Transneft; United Aircraft Corporation; Uralvagonzavod; Vnesheconombank (VEB); and VTB Bank (the "11").

Initially these controls were only intended to be in place for a single year in response to Russia's incursions into Ukrainian territory, but they have been renewed repeatedly by the EU due to lack of progression in the implementation of the 'Minsk Agreements', most recently in December 2018 with an extension until 31 July 2019.

Importantly, they also apply to (A) any legal person established outside of the EU who is more than 50% owned (directly or indirectly) by one of the entities specifically identified by the Sectoral Sanctions, or acting at their direction, and (B) any legal person acting at the direction of an entity referred to under A (or that is specifically identified).

Article 5 prohibits EU legal persons from direct and indirect dealings which comprise of "*transferable securities and money-market instruments with a maturity exceeding 90 days*" issued by any entity caught within the scope of the Sectoral Sanctions, including the 11. Initially this 90 day period concerned securities/instruments issued after 1 August 2014, however subsequent amendments have reduced this to 30 days, for those securities/instruments issued after 12 September 2014, in addition to prohibiting "*directly or indirectly*" making or being part of "*any arrangement to make new loans or credit with a maturity exceeding 30 days*" to those entities targeted by the Sectoral Sanctions (save for in certain number of specified circumstances). EU guidance suggests a broad interpretation of 'loans or credit', which may include extended payment terms. Importantly, EU guidance further confirmed that "*Article 5 is carefully designed to ensure that EU subsidiaries of targeted entities do not become targeted entities themselves,*" which the UK is in agreement with.

TRAVERS SMITH

THE UK SANCTIONS FRAMEWORK POST-BREXIT

Following a consultation undertaken by the Government in 2017, the UK put in place its own sanctions framework on 23 May 2018 to enable the UK to impose, update and lift economic and other sanctions, in addition to money laundering regulations, after the UK departs from the EU in the form of the Sanctions and Anti-Money Laundering Act 2018 ("SAMLA"). At present, the UK uses the powers as set out in the European Communities Act ("ECA") 1972. As currently planned, the EU Withdrawal Act 2018 will repeal the ECA at 11pm on the 29 March 2019 and, in the event of no-deal Brexit, sanctions-making powers under SAMLA will come into force at the same time to enable the UK to comply with its various international obligations under the global sanctions regime.

On 1 February 2019, the Office of Financial Sanctions Implementation ("OFSI") and HM Treasury released guidance on how the UK would implement sanctions if the UK leaves the EU without a deal. As international law requires, the UK will implement UN sanctions in domestic law after the UK leaves the EU; if there is no deal with the EU, the current position of the Government is that the UK *"will look to carry over all EU sanctions at the time of [the UK's] departure."*

THE POSSIBLE IMPACT OF NO-DEAL ON THE SECTORAL SANCTIONS

As it stands, if the draft Withdrawal Agreement that has been negotiated with the EU is agreed prior to the 29 March a transition period until at least 31 December 2020 would follow, which includes the continued application of the Common Foreign and Security Policy ("CFSP"). The UK would therefore, at least until the end of this period, be required to implement and maintain EU sanctions under the CFSP. The Sectoral Sanctions would in turn continue to apply.

In the event of a no-deal exit, the UK will become a non-EU entity for the purposes of the Sectoral Sanctions, including Article 5. This means that UK companies that are more than 50% owned (directly or indirectly) by one of the 11 may potentially be in scope of the Sectoral Sanctions.

There are a number of risks for these entities (and those who do business with them) associated with this potential new status, including reputational, commercial and legal concerns related with coming in scope of the EU's sanctions regime. This may make it more difficult to conduct business seamlessly in the future and will require a careful analysis of previous reps and warranties that have been made in respect to sanctions status. Entities and individuals operating and living within the EU's regulatory perimeter will also need to review their future and present relationship with any UK entities that become subject to Article 5 restrictions, including potentially updating sanctions and export policies and procedures. It goes without saying that the Government will not be comfortable with UK entities being suddenly considered a sanctions risks by the EU, even if this is just on the grounds of their new post-Brexit status.

WHAT NEXT FOR THE SECTORAL SANCTIONS

Irrespective of whether a deal is reached with the EU or not, the Sectoral Sanctions will be relevant for UK and EU entities moving forward although in a no-deal scenario there will be a significantly shorter period of time to ensure that compliance programmes are updated as and where necessary. If a deal is agreed between the UK and the EU, it is possible that the Sectoral Sanctions will no longer be in place by the end of the transition period, although this is unlikely given there has been no progress in implementing the 'Minsk Agreements.'

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