
Expanded Sanctions Target Russia's Defense Industry

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The United States, European Union and Canada each took steps recently to expand sanctions against Russia, including the targeting of major defense companies and the addition of export controls. These designations and export control steps have implications for defense contractors and brokers.

The Office of Foreign Assets Control ("OFAC") listed the following Russian defense-sector companies as Specially Designated Nationals ("SDNs") effective July 16, 2014:

- Almaz-Antey Corp.
- Federal State Unitary Enterprise State Research and Production Enterprise Bazalt
- JSC Concern Sozvezdie
- JSC MIC NPO Mashinostroyenia
- Kalashnikov Concern
- KBP Instrument Design Bureau
- Radio-Electronic Technologies
- Uralvagonzavod.

In addition, on July 29, 2014, OFAC designated the United Shipbuilding Corporation, which designs and repairs both military and commercial ships in Russia.

New transactions with these Russian companies by U.S. companies, citizens or permanent residents or persons in the United States are prohibited. As a consequence, transactions in dollars in which funds transfers clear through the U.S. banking system are subject to blocking as well. In addition, the sanctions apply to any company owned 50 percent or more by one of these manufacturers.

These designations, however, do not apply to equipment previously manufactured by these companies and already purchased and fully paid for. Such equipment is not blocked and may be possessed and used by persons subject to U.S. jurisdiction. Further, the sanctions do not prohibit new sales or lease

transactions for such equipment in the secondary market. For example, according to OFAC guidance, if a U.S. person owns 100 AK-47 rifles originally manufactured by Kalashnikov Concern and purchased outright before July 16, 2014, these rifles may be re-sold in the secondary market so long as the sanctioned Russian companies or other SDNs are not part of the transaction.

If equipment has been ordered or acquired from one of these Russian companies, but money is still owed, the items may be blocked. Depending on the transaction, the sanctioned companies may continue to have an interest in the equipment. OFAC has recommended that any purchaser in such a situation seek guidance on whether the U.S. government would consider the items to be blocked.

In addition to the OFAC SDN designations, these nine companies have been added to the U.S. Bureau of Industry and Security (“BIS”) Entity List. Any export or re-export to these companies of goods, software or technology subject to the Export Administration Regulations (“EAR”) is now prohibited without a license, with a presumption that any such license request will be denied. Jurisdiction is based on U.S. content. Non-U.S. persons acting outside of the United States are subject to the prohibition if exporting or re-exporting to these companies items that are subject to the EAR.

The U.S. State Department’s Directorate of Defense Trade Controls (“DDTC”) has not yet issued a new policy statement concerning these companies. Exports of defense articles and defense services to Russia, however, are subject to a policy of denial. Brokering requests related to the resale of previously purchased defense articles from defense sector companies may be approved, although companies are advised to contact DDTC for guidance.

Actions in Other Jurisdictions

To date, the European Union (“EU”) has designated only one entity within the arms and materiel industry, Almaz-Antey Corp. The EU, however, has placed restrictions on exports of dual-use goods and technology that could be intended for a military end use/end user in Russia. The sale, supply, transfer or export directly or indirectly to a person in Russia or for use in Russia is prohibited. Further, the EU has prohibited technical assistance and financing/financial assistance relating to items on the Common Military List or dual-use goods that could be used for a military end use or end user, as well as the provision to, manufacture or maintenance for, or use of such items by a Russian person or in Russia. Pre-existing contract obligations, however, may be authorized.

Canada has designated eight of the same entities that the U.S. designated for operating in the arms and materiel industry. Property of the designated entities that is within Canada or the possession of a Canadian person is now blocked.

Sanctions and export controls continue to evolve in response to events in Ukraine and Russia. The defense manufacturing and materiel sector in Russia likely will continue to be a target of sanctions by the U.S. and other western governments.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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