

*****ALERT*******U.S. GOVERNMENT IMPOSES SANCTIONS ON ROSTEC STATE CORPORATION – HOW THIS AFFECTS U.S. IMPORTERS**

On September 12, 2014, the Office of Foreign Assets Control (OFAC), Department of the Treasury, added the Rostec State Corporation (Rostec) to the Sectoral Sanctions Identification List. As explained in detail below, importation of firearms, ammunition, and other defense articles from Russia could be affected by the sanctions imposed on Rostec.

BACKGROUND

On March 20, 2014, the Administration issued Executive Order 13662 titled “Blocking Property of Additional Persons Contributing to the Situation in Ukraine.” The Order references the actions of the Russian Federation that continue to undermine democratic processes and institutions in Ukraine that threaten its peace, security, and stability. The order states that these actions present a threat to the national security and foreign policy of the United States and directs the Secretary of the Treasury, in consultation with the Secretary of State, to block the property and interests in property of persons determined to operate in certain sectors of the Russian Federation economy, such as financial services, energy, metals and mining, engineering, and defense and related material. The full text of E.O. 13662 is [here](#).

The sanctions imposed under E.O. 13662 have been implemented by OFAC pursuant to its delegated authority. These sanctions, referred to as “sectoral sanctions,” are different from OFAC’s designation of an entity as a Specially Designated National (SDN). As we advised you in our July 23, 2014, Client Alert, relating to designation of Kalashnikov Concern as a SDN, OFAC’s designation of an entity as a SDN results in blocking all property and interests of the entity that comes under U.S. jurisdiction. Blocking for such an entity immediately imposes an across-the-board prohibition against transfers or transactions of any kind involving the property. Conversely, sectoral sanctions are not as broad as SDN sanctions and are specifically defined in a series of OFAC directives.

OFAC has issued four directives implementing the sectoral sanctions imposed by E.O. 13662. The directive relevant to importers of defense articles is **Directive 3**, issued September 12, 2014, which relates to the defense and related materiel sector of the Russian Federal economy. The directive prohibits the following activities by a U.S. person or within the United States, unless licensed or authorized by OFAC: “[A]ll transactions in, provision of financing for, and other dealings in new debt of longer than 30 days maturity of persons determined to be subject to this Directive, their property, or their interests in property.” The full text of Directive 3 is [here](#).

OFAC has also made it clear that the prohibitions imposed under the directives extend to entities owned 50% or more by an entity identified in a directive. This position is included in a question and answer on OFAC’s website, as follows:

373. Do the prohibitions imposed pursuant to the Directives also extend to entities owned 50 percent or more by one or more entities identified by these Directives, as per revised guidance OFAC issued on August 13, 2014?

Yes, these prohibitions apply to the named persons, their property, and their interests in property, which includes entities owned 50 percent or more by one or more persons identified as subject to the Directives. [9-12-2014]

Questions Related to Sectoral Sanctions Under Executive Order 13662 can be found on OFAC's website [here](#).

On August 13, 2014, OFAC provided guidance on the 50% rule referenced in the question above. The guidance document states that persons whose property and interests in property are blocked by OFAC are considered to have an interest in all property of an entity in which such blocked persons own, whether individually or in the aggregate, directly or indirectly, a 50% or greater interest. Consequently, OFAC advises, any entity owned 50% or more by one or more blocked persons is itself considered to be a blocked person. This position applies whether or not the entity itself is listed in an OFAC list or directive. The complete text of the OFAC guidance on the 50% rule can be found [here](#).

OFAC publishes the Sectoral Sanctions Identifications List, a complete list of the entities subject to sectoral sanctions listed under the directive(s) that apply to the entity. The following listing appears under Directive 3:

ROSTEC (a.k.a. ROSTEC STATE CORPORATION; a.k.a. RUSSIAN TECHNOLOGIES; a.k.a. RUSSIAN TECHNOLOGIES STATE CORPORATION FOR ASSISTANCE TO DEVELOPMENT, PRODUCTION AND EXPORT OF ADVANCED TECHNOLOGY INDUSTRIAL PRODUCT; a.k.a. STATE CORPORATION FOR ASSISTANCE TO DEVELOPMENT, PRODUCTION AND EXPORT OF ADVANCED TECHNOLOGY INDUSTRIAL PRODUCT ROSTEKHNOLOGII; a.k.a. STATE CORPORATION ROSTEKHNOLOGII; a.k.a. STATE CORPORATION ROSTEKHNOLOGII), 24 Usacheva ul., Moscow 119048, Russia; 21 Gogolevsky Blvd., Moscow 119991, Russia; Website www.rostec.ru; Email Address info@rostec.ru; Executive Order 13662 Directive Determination - Subject to Directive 3; Registration ID 1077799030847 (Russia); Tax ID No. 7704274402 (Russia); Government Gazette Number 94137372 (Russia). [UKRAINE- EO13662].

ROSTEC STATE CORPORATION (a.k.a. ROSTEC; a.k.a. RUSSIAN TECHNOLOGIES; a.k.a. RUSSIAN TECHNOLOGIES STATE CORPORATION FOR ASSISTANCE TO DEVELOPMENT, PRODUCTION AND EXPORT OF ADVANCED TECHNOLOGY INDUSTRIAL PRODUCT; a.k.a. STATE CORPORATION FOR ASSISTANCE TO DEVELOPMENT, PRODUCTION AND EXPORT OF ADVANCED TECHNOLOGY INDUSTRIAL PRODUCT ROSTEKHNOLOGII; a.k.a. STATE CORPORATION

ROSTEKHNLOGII; a.k.a. STATE CORPORATION ROSTEKHNLOGII), 24 Usacheva ul., Moscow 119048, Russia; 21 Gogolevsky Blvd., Moscow 119991, Russia; Website www.rostec.ru; Email Address info@rostec.ru; Executive Order 13662 Directive Determination - Subject to Directive 3; Registration ID 1077799030847 (Russia); Tax ID No. 7704274402 (Russia); Government Gazette Number 94137372 (Russia). [UKRAINE- EO13662].

The complete Sectoral Sanctions Identifications List is [here](#).

OFAC JURISDICTION AND PENALTIES

OFAC has sweeping jurisdiction over U.S. persons and persons subject to U.S. jurisdiction. This includes U.S. citizens and permanent resident aliens (“green card” holders) whether in the U.S. or abroad, companies organized and formed under U.S. law, and any individual or organization physically located in the U.S. at the time of the activity, regardless of nationality. In addition to these direct controls, OFAC sanctions also prohibit the facilitation of foreign trade with targets of U.S. sanctions. The facilitation prohibitions prevent U.S. persons from undermining sanctions through indirect support and apply to approving, financing, guaranteeing or otherwise assisting foreign trade with a sanctions target, changing policies or procedures to permit foreign affiliates to engage in activities with a sanctions target that previously required U.S. approval, and even referring declined business opportunities to a foreign party.

The penalties for violating OFAC sanctions are substantial. Pursuant to the International Emergency Economic Powers Act (IEEPA), the underlying statute for the Ukraine sanctions, any person who causes a violation of the sanctions can be held liable for both civil and criminal penalties. Civil penalties can be up to \$250,000 per violation or twice the transaction value, whichever is greater. Criminal penalties can be up to \$1 million per violation or twice the transaction value, whichever is greater, and up to 20 years imprisonment, or both. In addition, OFAC violations also lead to denial or debarment of export privileges under the International Traffic in Arms Regulations. Voluntary self-disclosures may mitigate the penalties, but we recommend consultation with legal counsel before undertaking such action.

It is also important to note that OFAC violations are subject to strict liability. This means that OFAC only has to prove a violation occurred. OFAC does not have to prove the U.S. person intentionally or knowingly violated the sanctions.

IMPACT OF DIRECTIVE 3 ON IMPORTERS

The listing of Rostec under Directive 3 affects importers of defense articles because Rostec has an ownership interest in several manufacturers of ammunition operating in the Russian Federation. Murom Apparatus Producing Plant and Tulammo (formerly known as Tula Cartridge Works) are both ammunition manufacturing plants in the Russian Federation. We are advised that both companies are partially owned by Rostec. As noted in our Alert of August 15, 2014, relating to ATF’s suspension of import permits for nine named Russian entities, there is an inter-connected

web of ownership of arms manufacturers in Russia. Accordingly, importers should inquire into the ownership of all manufacturers in Russia with whom you are doing business.

If a determination is made that Rostec holds a 50% or greater interest in a particular entity, Directive 3 will prohibit transactions in, provision of financing for, and other dealings “in new debt of longer than 30 days maturity of persons determined to be subject to this Directive.” OFAC advises that Directive 3 applies only to debt issued to Rostec and other listed entities. The Directive does not apply to debt held by or issued to a U.S. company under contract with Rostec. Consequently, OFAC advises that contracts with Rostec that authorize deferred payment by the U.S. purchaser (e.g., payment may be made within a period of time following shipment) are not debt issued to or held by Rostec and are therefore unaffected by Directive 3.

New debt issued to Rostec and other listed entities is subject to the prohibitions of Directive 3 if the maturity exceeds 30 days. It is important to note that OFAC interprets “debt” to include both money and goods. Therefore, if a U.S. purchaser pays Rostec or any other listed entity in advance for product, title in the product must pass to the U.S. purchaser within 30 days of the date on which the U.S. purchaser sent payment to Rostec.

THE BOTTOM LINE

Importers dealing with Russian manufacturers or sources of defense articles should ensure their transactions are not blocked pursuant to the sectoral sanctions imposed under Directive 3, which OFAC issued on September 12, 2014. It is important to consider the following:

1. Importers should obtain information about the ownership of the Russian manufacturer of the firearms, ammunition, or other defense article to be imported into the United States.
2. If Rostec (or another Russian entity subject to the sectoral sanctions) has no ownership interest in the company, the sectoral sanctions do not apply to the transaction. Conversely, if Rostec (or another Russian entity subject to the sectoral sanctions) has a greater than 50% ownership interest, Directive 3 may apply.
3. Directive 3 applies if the transaction involves financing for and other dealings in new debt of longer than 30 days maturity. Such financing or debt must be issued to Rostec (or a related company in which Rostec has a qualifying ownership interest), as opposed to a U.S. company, to be prohibited under Directive 3. Contracts that provide for a U.S. purchaser to make payment at some date after shipment or sale are not debt issued to Rostec (or a related company) and are not prohibited by Directive 3.
4. Contracts allowing Rostec (or a related company in which Rostec has a qualifying ownership interest) to ship products to a U.S. purchaser more than 30 days after any portion of the purchase price is sent to Rostec would amount to a debt prohibited under the sanctions. As the clock does not stop running until title to the product passes to the U.S.

purchaser, U.S. purchasers must be careful of transactions that require advance or partial payment to Rostec or a Rostec-owned entity. The U.S. company must have evidence of the title change and the date the title change occurs. Such evidence may include a bill of lading, purchase order, or contract.

5. If the restrictions of Directive 3 cannot be avoided (e.g., the contract has already been negotiated and cannot be altered and/or the goods are in the process of shipment to the U.S.), importers may seek a license from OFAC specifically authorizing the transaction. Companies who wish to apply for an OFAC license may contact OFAC or legal counsel for assistance.
6. Companies entering into new contracts with Russian manufacturers should draft agreements to avoid the prohibitions of Directive 3.

The above analysis is for informational purposes only and is not intended to be construed or used as legal advice. Receipt of this alert does not establish, in and of itself, an attorney-client relationship.

Questions about this alert can be directed to:

Johanna Reeves — 202.715.9941 | jreeves@reevesdola.com

Teresa Ficaretta — 202.715.9183 | tficaretta@reevesdola.com