

# UK Secondary Sanctions? The UK Broadens Its Designation Criteria To Target Foreign Persons With Exposure to the Russian Government and Military-Industrial Base

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If you have any questions regarding the matters discussed in this memorandum, please contact the attorneys listed on the last page or call your regular Skadden contact.

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On 31 July 2024, the UK government broadened its Russian sanctions regime, giving the government express power to impose sanctions on persons who provide financial services, or make available funds, economic resources, goods or technology to persons involved in obtaining a benefit from or supporting the Russian government. The change is principally intended to allow the UK government to designate foreign financial institutions that facilitate transactions on behalf of, or in support of, a broad range of specified sectors of strategic significance to the Russian government, even if those institutions are outside the UK's jurisdiction.<sup>1</sup>

The changes to the Russia (Sanctions) (EU Exit) Regulations 2019 (hereafter Russia Regulations) were effected through enactment of the Russia (Sanctions) (EU Exit) (Amendment) (No 3) Regulations 2024 (Amending Regulations).

Although the Amending Regulations have not been billed as “secondary sanctions” measures, as explained in this alert, the expanded designation authority broadly aligns with the secondary sanctions provisions in the US under Executive Order (EO) 14114, which President Biden issued on 22 December 2023.

How aggressively the UK government will apply its expanded authority — and whether it will seek to enact additional secondary sanctions-like measures in the future — remains to be seen. Regardless, global financial institutions with continued exposure to Russia may wish to consider whether their existing sanctions compliance processes can effectively identify and mitigate the risks stemming from that exposure in light of the Amending Regulations.

## Amendments to the Designation Criteria Under the Russia Regulations

The Russia Regulations allow the UK government to impose a number of different sanctions, including asset freezing and/or correspondent banking and payment processing sanctions, if the target satisfies one or more of the relevant designation criteria. These criteria have been expanded incrementally since Russia's invasion of Ukraine in 2022 to make the UK sanctions more effective in fulfilling their dual purposes of: (i) encouraging Russia to cease actions destabilising Ukraine or undermining or threatening the territorial integrity, sovereignty or independence of Ukraine; and (ii) promoting the payment of compensation by Russia for damage, loss or injury suffered by Ukraine as a result of the invasion.

Regulation 6(1) of the Russia Regulations provides that no person can be designated under the UK sanctions regime unless the UK government: (i) has reasonable grounds to suspect that that person is an “involved person” and (ii) considers that the designation of that person is appropriate, having regard to the purposes of the UK sanctions regime and the likely significant effects of this person being designated.

<sup>1</sup> This client alert is for informational purposes only and does not constitute legal advice. Complex assessments often have to be made as to which sanctions regime applies in any given instance, given the multinational touch points of many entities and individuals. In that regard, given the complex and dynamic nature of these sanctions regimes, there may be developments not captured in this summary. Moreover, while the summary was accurate when written, it may become inaccurate over time given developments. For all of these reasons, you should consult with a qualified attorney before making any judgments relating to sanctions, as there are potentially severe consequences for failing to adhere fully to sanctions restrictions.

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Regulation 6(2) further defines an involved person as, *inter alia*, a person who “is or has been involved in destabilising Ukraine or undermining or threatening the territorial integrity, sovereignty or independence of Ukraine, or obtaining a benefit from or supporting the Government of Russia”.

Regulations 6(3) and following set out the categories of involved persons. The Amending Regulations expand the definition of a person involved in destabilising Ukraine or undermining or threatening the territorial integrity, sovereignty or independence of Ukraine to include:

- Any persons owning or controlling, directly or indirectly, or working as a director (whether executive or non-executive), trustee or other manager or equivalent of, an entity that could be considered an involved person under any of the previous categories under Regulation 6(3); and
- Any persons having the right, directly or indirectly, to nominate at least one director (whether executive or non-executive), trustee or equivalent of, an entity that could be considered an involved person under any of the previous targeted categories of person.

Perhaps most importantly, the new Regulation 6(4)(f) expands the definition of an involved person obtaining a benefit from or supporting the Russian government to include any person providing financial services, or making available funds, economic resources, goods or technology, to a person or an entity falling within any of the previous categories under Regulation 6(4). This includes persons carrying on business in a sector of strategic significance to the Russian government, which includes the defence, electronics, energy and financial services sectors.

Finally, the new Regulation 6(4A)(m) broadens the definition of a person involved in destabilising Ukraine or undermining or threatening the territorial integrity, sovereignty or independence of Ukraine or obtaining a benefit from or supporting the Russian government if they work for, or are affiliated to, the Russian government, to include any person providing financial services, or making available funds, economic resources, goods or technology, to a person or entity falling within any of the previous categories under Regulation 6(4A). This includes a broad range of Russian politicians and officials working for the Russian government, as well as directors and managers of entities affiliated with the Russian government.

## Impact of the Amendments

The amendments represent an incremental but potentially significant expansion of the UK government’s ability to designate persons for activities which fall inside *and outside* of the UK’s

legal jurisdiction. Specifically, the UK government has explained that the additions of new Regulations 6(4)(f) and 6(4A)(m) are intended to expand “the criteria under the Regulations to designate entities, *including foreign financial institutions* that facilitate transactions on behalf of, or in support of, specified sectors of strategic significance to the Russian government. This in line with G7 commitments to further curtail Russia’s use of the international financial system which Russia is using to facilitate its war in Ukraine” (emphasis added).

Importantly, while the UK government has not described them as “secondary sanctions”, the scope and apparent purpose of the Amending Regulations are similar to those of the US secondary sanctions implemented as part of EO 14114. So-called “secondary sanctions” are measures that principally target non-US persons for engaging in certain enumerated activities even if these activities have no US nexus that would create US sanctions jurisdiction. What further distinguishes secondary sanctions from “primary sanctions,” is that engaging in activities covered by secondary sanctions is not a violation of law punishable by a civil or criminal penalty, but rather may result in the imposition of certain types of sanctions on the offending person.

The severity of the sanctions varies from relatively minor (*e.g.*, restrictions on the foreign person’s access to services provided by the Export-Import Bank of the United States) to severe (*e.g.*, designating the foreign person and adding them to the List of Specially Designated Nationals and Blocked Persons). These sanctions are not self-executing, however — the US government must first determine that a non-US person has engaged in sanctionable conduct and that sanctions are warranted. The US has used secondary sanctions in several of its sanctions programs, most notably those directed at Russia and Iran.

In relevant part, EO 14114 makes it sanctionable for non-US financial institutions to engage in or facilitate “significant transactions” or provide any services involving Russia’s military-industrial base. The US government interprets the term “Russia’s military-industrial base” to include:

- All persons sanctioned under EO 14024 (a 2021 executive order that authorises the imposition of sanctions on individuals and entities that have engaged in a broad range of activities with respect to Russia and the Russian government, and which represents the primary designation authority in the Russian Harmful Foreign Activities Sanctions program); and
- More broadly, any person operating in the technology, defense and related materiel, construction, aerospace and manufacturing sectors of the Russian economy, as well as other sectors that may be added in the future.

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EO 14114 authorizes the imposition of full blocking sanctions or narrower correspondent or payable-through account restrictions on non-US financial institutions that engage in the activities covered by EO 14114.

There is thus clear overlap between the scope of EO 14114 and the Amending Regulations, specifically Regulation 6(4)(f). Moreover, the Amending Regulations build on the UK government's already broad designation powers, which it has used to target non-Russian companies and individuals since February 2022. Companies from a range of jurisdictions including the UK, China, Cyprus, Kyrgyzstan, Israel, Syria, Türkiye and the United Arab Emirates have been designated under the Russia

Regulations, some for supplying munitions, machine tools, microelectronics, logistics or other supplies to the Russian military-industrial complex.

It remains to be seen how aggressively the UK government will utilize its new powers. However, foreign financial institutions that continue to do business involving Russia, especially in circumstances where they also depend on access to the global financial system and utilize GBP payments, should consider assessing the risks posed by that continued business in light of the powers conferred by the Amending Regulations and, where appropriate, taking action to mitigate those risks.

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