

Navigating international sanctions



Freshfields Bruckhaus Deringer



Navigating international sanctions

Economic and trade sanctions have become a favoured geopolitical tool of governments. The rules are complex, ever evolving, and the risks of violation can be high.

Every company operating across borders needs to plan for the potential effect of sanctions on their business, how to manage the risks, and how to position itself to operate safely by taking decisions that make business sense.

On the positive side, companies that properly formulate their objectives, plan their strategy and implement it well will benefit from being in a better position to navigate sanctions when they hit and may well have a competitive advantage.



For an overview to sanctions, click on the thumbnail to open a video in your web browser.



Frequently asked questions

Some frequently asked questions regarding sanctions.

What are sanctions?

Economic and trade sanctions are restrictions that governments impose on certain types of transactions with targeted countries or persons, as a tool to achieve foreign policy or national security goals. Sanctions often are imposed in an effort bring about a change with regard to armed conflict, international terrorism, the spread of weapons of mass destruction, narcotics trafficking, violations of international law, human rights or policies that do not respect the law or democratic principles. They aim to fulfil these political objectives as well as to restore international peace and security and to enforce security interests without resorting to military action. They are seen by many governments to be an important and valuable tool in a broad range of international crises.

How do sanctions get imposed?

In the US – most US sanctions are imposed by the US President, under general statutory authority to respond to international crises, through an Executive Order. In some cases, US Congress enacts legislation imposing sanctions on specific countries or persons. Executive Orders and sanctions statutes are generally implemented by the US Treasury, State or Commerce Departments through regulations or various other administrative measures. These executive branch departments have broad authority to investigate and impose civil penalties on persons found to have violated sanctions. The US Department of Justice and US Attorneys offices, and certain state and local prosecutors have the authority to seek criminal penalties through the US courts. Sanctions are primarily a matter of federal, not state, law. However, some state banking regulators have taken an active approach towards economic sanctions, and US Congress has authorised certain limited economic sanctions measures by state and local governments.

In the EU – sanctions are either imposed the Council in implementation of Resolutions adopted by the UN Security Council under Chapter VII of the UN Charter or within the framework of the Common Foreign and Security Policy (CFSP). With regard to these latter measures, the Council first adopts a CFSP Decision under Article 29 of the TEU. The measures foreseen in that Council Decision are either implemented at EU or at national level. Measures such as arms embargoes or restrictions on admission are implemented directly by the Member States, which are legally bound to act in conformity with CFSP Council Decisions. Other measures interrupting or reducing, in part or completely, economic relations with a third country, including measures freezing funds and economic resources, are implemented by means of a Regulation, adopted by the Council, acting by qualified majority, on a joint proposal from the High Representative of the Union for Foreign Affairs and Security Policy and the Commission, under Article 215 of Functioning of the European Union.

The European Parliament has to be informed. Such Regulations are binding and directly applicable throughout the EU, and they are subject to judicial review by the Court of Justice and the General Court in Luxembourg. CFSP Council Decisions providing for restrictive measures against natural and legal persons are also subject to judicial review.

Who most frequently imposes sanctions?

- › United States
- › European Union
- › EU Member States (where the EU does not have exclusive competence)
- › Other countries
- › UN Security Council (Resolutions have to be implemented by member states)
- › Other regional bodies

What are sanctions?

How do sanctions get imposed?

Who most frequently imposes sanctions?



Frequently asked questions (continued)

Some frequently asked questions regarding sanctions.

How do sanctions get lifted?

In the US the lifting of US sanctions can be quite straightforward – if they were imposed by the President acting on his general authority, they can also be lifted quite rapidly under that same authority. Sanctions imposed, in whole or in part, on the basis of specific statutes enacted by US Congress can be much more difficult and slower to lift. Often, the executive branch can only go so far to lift or waive such sanctions and a complete lifting will require new action by Congress. This is a difficult and uncertain process at best.

In the EU there are two ways for sanctions to get lifted; either the legal instruments from the outset provide for an expiration date (ie the sanctions imposed expire automatically at a certain point in time if they are not renewed or amended as appropriate), or the sanctions are repealed if the Council deems that their objectives have been met. In order to ensure that the need for renewal of restrictive measures is discussed within an appropriate period of time EU sanctions regulations usually contain either an expiration or a review clause.

What type of sanctions can be imposed?

- Arms embargoes
- Financial sanctions
 - Prohibitions on the provision of financing or **financial services to targeted countries or persons**
 - Restrictions on the raising of new equity or debt capital by **targeted companies**
 - Bans on the provision of specific services (brokering, financial services, technical assistance)
- Trade sanctions
 - Export and/or import bans (trade sanctions generally applicable to specific products such as oil, timber or diamonds)
 - Prohibitions on investment, payments and capital movements
 - Withdrawal of tariff preferences
 - Flight bans
- So-called ‘Smart sanctions’, ie sanctions which targets pecific individuals, groups or entities (‘persons’)
 - Freezing of all funds and economic resources of the targeted persons
 - Prohibition on making funds or economic resources available (directly or indirectly) to or for the benefit of targeted persons
 - Prohibition on engaging in transactions or dealings with the targeted persons
 - Visa or travel bans on targeted individuals
- Most sanctions programs broadly prohibit circumvention which means doing indirectly, or supporting other parties in doing, activities that would be prohibited if done directly

Who and what can be targeted?

- States (including their public authorities)
- Individuals, ie natural persons
- Legal persons, entities or bodies
- Organisations
- Vessels and aircraft

What are the main risks from sanctions for companies?

- Business disruption – governments may feel compelled in a crisis to suddenly cut off substantial flows of trade and commerce
- Loss of assets and other investment in emerging markets that become targeted by sanctions
- Potentially severe penalties – a serious breach of sanctions is generally a criminal offence, with large fines payable and the possibility of prison sentences for individuals
- Reputational damage
- Time and distraction for management to deal with sanctions breaches, particularly if there is risk of regulatory or reputational consequences

How do sanctions get lifted?

What type of sanctions can be imposed?

Who and what can be targeted?

What are the main risks from sanctions for companies?



Frequently asked questions (continued)

Some frequently asked questions regarding sanctions.

Who must comply with EU sanctions?

EU sanctions apply to all EU nationals, including entities incorporated or constituted under the law of an EU member state – regardless of where they are doing business inside or outside the EU. They also apply to all business done by EU and non-EU persons in whole or in part within EU territory, including its airspace and on any aircraft or vessel under an EU member state’s jurisdiction. For EU sanctions to apply, it is therefore sufficient that an EU national is involved or that the parties partially act within the EU.

What do EU sanctions generally look like?

The Guidelines on implementation and evaluation of restrictive measures (sanctions) in the framework of the EU Common Foreign and Security Policy published by the Council of the European Union in 2012 and 2013 (11205/12 and 9068/13) address a number of general issues and present standard wording and common definitions that are used in the EU legal instruments implementing restrictive measures. Among others these include asset freezes, export controls, visa or travel bans, arms embargoes.

Who must comply with US sanctions?

US sanctions apply to US persons – that is, any US citizen (including dual nationals), permanent resident (‘green card’ holder), any entity formed under US law, any person in the US or any person taking or causing action within the US. This includes any employee, officer or director of a US or non-US company who is a US citizen or permanent resident, wherever in the world they are. In relation to Cuba and Iran, non-US entities majority owned or controlled by US persons are directly required to comply with US sanctions. US sanctions also apply to non-US persons where there is a sufficient US nexus – for example, sourcing goods from the US or otherwise involving US persons in exports or other transactions with sanctioned countries.

What do US sanctions generally look like?

Territorial embargoes
For example, the almost complete export and import embargoes against Cuba, Iran, Syria and Sudan.

Secondary sanctions
Extraterritorial sanctions providing for a range of penalties for non-US persons who engage in certain specified activities, for example activities involving Iran’s energy, military or shipping sectors.

Facilitation
General prohibitions against evasion, facilitation, conspiracy and causing another person to violate any prohibition under the sanctions .

USD transactions
Electronic payments denominated in US dollars are prohibited if targeted countries or persons are involved in any related transactions. This prohibition can apply even if the payments are initiated outside US, on the basis that almost all US dollar payments anywhere in the world will indirectly clear through the US.

Blocking (asset freezing)
Any funds or other assets of individuals or entities covered by US blocking (asset freezing) sanctions must be ‘blocked’ (frozen) if they:

- › come within US jurisdiction; or
- › come into possession or control of a US person.

Blocking applies to various categories of sanctioned persons, including several targeted governments, and all of the individuals and entities on the primary US sanctions list (the ‘SDN list’). Any blocking of assets must be reported promptly to the US Treasury Department. What are the potential penalties?

What are the potential penalties?

EU
EU Regulations allocate responsibility for penalties for sanctions violations to the EU Member States, rather than EU institutions. In general, EU sanctions regulations provide that EU Member States shall lay down rules for effective, proportionate and dissuasive penalties for infringements of the relevant regulation and shall take all measures necessary to ensure that they are implemented. Penalties therefore vary from Member State to Member State.

- US**
Civil penalties
- › Up to \$250,000 or double the transaction value
 - › Forfeiture of goods involved or forfeiture of profits from the transaction
 - › Addition to the SDN list

Criminal penalties (for wilful violations)
› Up to 20 years in prison

› Fine up to the greater of \$1m and twice the pecuniary gain or loss

Iran-specific penalties include
› Exclusion from US markets

› Denial of US loan facilities

› Loss of US correspondent banking accounts

Who must comply with EU sanctions?

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Who must comply with US sanctions?

What do US sanctions generally look like?

What are the potential penalties?



Glossary of common terms

Here are some commonly used terms in the context of sanctions.

Asset Freeze

Most US and EU sanctions programs have as one component the freeze of the assets of certain designated individuals or entities. Over many decades, asset freezing has been a tool to impose economic pressure on the targets of sanctions, to ensure that funds and other assets of targeted persons located in the country imposing sanctions could not be used to fund harmful activities, and to build up a body of frozen assets to be used as a bargaining chip in any ultimate settlement of a dispute with the targeted persons under the sanctions.

Generally, an asset freeze immediately imposes an across-the-board prohibition on transfers or dealings of any kind with regard to the property. Legal title to the frozen assets generally remains with the targeted person, but the persons in possession or control of those assets are prohibited from turning them over or making them available to the targeted person. In other words, the targeted person cannot exercise their normal powers and privileges associated with ownership of the frozen assets without authorisation from the relevant sanctions regulator.

Blocking

Term used in US sanctions to refer to asset freezing.

Blocking Laws

EU and US sanctions often go hand-in-hand in order to maximise their impact on targeted countries. But sometimes the two entities have different objectives, and as a result their sanctions regimes are incongruent. In this situation, compliance with one sanctions regime contravenes the blocking laws of another jurisdiction.

Circumvention Provisions

Provisions which prohibit the knowing and intentional participation in activities the object of which is to carry out indirectly or through other persons any transactions or actions that would be prohibited by the sanctions if carried out directly. As a consequence, an entity incorporated in an EU Member State may not, inter alia, use a non-EU company that it controls to carry out a transaction that the EU entity would be prohibited from carrying out itself. Furthermore, the EU entity may not give the non-EU company instructions to such effect or structure a particular transaction in a way to avoid or evade EU sanctions.

Commerce Control List

The list of goods and technologies specially controlled under US export control rules. It includes many of the same items as are on the EU Dual Use List and also includes a broad range of additional items.

Deemed Export

Under US export controls, an ‘export’ of software or technology may be ‘deemed’ to take place when it is released or made available to a non-US national either within or outside the United States. The software or technology may be ‘deemed’ to have been exported to the country of nationality of the non-US individual who has been given access to that software or technology.

Dual Use Goods

Describes items, including software and technology, which can be used in both civil applications and in military or other sensitive applications. For example, dual use items include all goods and technologies which can be used for both ordinary commercial applications and can be used to assist in the manufacturing of nuclear weapons or weapons of mass destruction.

EAR

Export Administration Regulations, the primary and broadest set of US export control regulations administered by the US Commerce Department.

Economic Resources

This term has a very broad meaning under EU sanctions and encompasses all assets of every kind, whether tangible or intangible, movable or immovable (such as goods, property or rights), which are not funds themselves but can be used to obtain funds, goods or services.

EU Person

All natural persons who are nationals of an EU Member State and all legal persons, entities or bodies which are incorporated or constituted under the law of an EU Member State.

Facilitation Provisions

Provisions which make it an offence for any US person to approve, finance, guarantee or otherwise ‘facilitate’ (support) any transaction by a non-US person where the transaction by that non-US person would be prohibited if performed by a US person.



Glossary of common terms (continued)

Here are some commonly used terms in the context of sanctions.

Freezing of Economic Resources

Preventing the use of economic resources to obtain funds, goods or services in any way, including, but not limited to, by selling, hiring or mortgaging them. See Asset Freeze above.

General and Specific Licences

A licence is an authorisation from the US Treasury or Commerce Department to engage in a transaction that otherwise would be prohibited under sanctions. There are two types of licences: general licences and specific licences. A general licence is publicly released and authorises a specified category of transactions for any person who meets its requirements, without the need to seek authorisation from the US government for each transaction. A specific licence is a written document issued by OFAC to a particular person or entity, authorising a particular transaction in response to a written licence application.

ITAR

International Traffic in Arms Regulations, the US military export control regulations administered by the US State Department.

Making Economic Funds Available

The concept of ‘directly or indirectly making available funds or economic resources’ is interpreted very broadly under EU sanctions. Pursuant to the CJEU rather than denoting a specific legal category of act, it encompasses all the acts necessary under the applicable national law if a person is effectively to obtain full power of disposal in relation to the asset or economic resource concerned.

OFAC

The US Treasury’s Office of Foreign Assets Control. OFAC is the US agency charged with planning and execution of economic and trade sanctions.

Specially Designated Nationals (SDN) list

A list published by OFAC of specially designated nationals and blocked persons. It includes individuals and companies that have been determined, through a rigorous government process, to have engaged in activities of concern covered by the relevant sanctions program – these are the ‘specially designated nationals’. For example, individuals, groups, and entities designated as terrorists and narcotics traffickers. The list also includes entities determined to be owned or controlled by, or acting for or on behalf of, certain US-embargoed countries or their governments – these are generally referred to as ‘blocked persons’.

Trade Controls

A commonly used shorthand reference for economic and trade sanctions and export controls.

US Nexus

A connection or link, often a causal one, to the United States or persons within the US. Generally, non-US persons carrying out a transaction outside the US may be required to comply with US sanctions if that transaction has a sufficient US nexus. This could include the sourcing of goods or services from the US, or other involvement of persons within the US, for an export to or other transaction with a country or person targeted by US sanctions.

US Person

Any United States citizen, permanent resident alien (‘green card’ holder), entity organised under the laws of the United States or any jurisdiction within the United States, or any person in the United States.

US Secondary Sanctions

In recent years, the US has imposed a broad range of extraterritorial sanctions under which non-US persons carrying out certain activities involving Iran may be penalised under US law, even if the non-US persons have no ties, contact or nexus to the US at all. The US government refers to these as ‘secondary’ sanctions because the penalties that can be imposed involve prohibitions on US persons dealing with the penalised persons. In other words, the secondary sanctions act by prohibiting US banks from lending, US companies from exporting, or other US persons from providing other services, to specified non-US persons.



Before sanctions

What should I know about my own business?

Am I legally required to know my business inside out?

As an officer or director of your company you should know your business as well as you can, including its potential exposure to economic and trade sanctions. But it’s impossible to know everything, particularly if you work for a large company.

It’s worth bearing in mind that, in some jurisdictions, your accountability for your business, as far as sanctions are concerned, goes beyond an officer’s or director’s general responsibility. German law for instance contains specific legal requirements for board members that could lead to personal liability or criminal prosecution for sanctions or export control violations.

Many jurisdictions accept that businesses follow a risk-based approach in ensuring compliance with sanctions, while others can impose sanctions penalties on a strict liability basis. In either case, this means that you should know those parts of your business that are particularly exposed to sanctions risk better than others.

Where should I focus my attention?

Your business could be exposed to sanctions through your territorial presence, your products and services, your employees or your business partners.

Territorial presence

Need to know
Sanctions must be complied with within the territory of the country that imposed the sanctions, so they typically apply to your employees in that state along with any subsidiaries incorporated there. Sanctions can also attach when employees from one country visit another. For example, US sanctions apply to anyone in the US, even temporarily. In addition to the sanctions law of the states in which you have operations or are located, you should also be aware of sanctions imposed by countries along your shipping routes. Even if none of your employees is involved in the shipping, it is possible that sanctions could apply with regard to the transport. Also, if your products transit through a sanctioned country, if a carrier or vessel used is on a sanctions list, or if the port is controlled by someone on a sanctions list, the shipment could be in violation of sanctions.

Products and services

Need to know
Sanctions and export controls often attach to the sale, purchase, transfer, import or export of products, and the provision of services, technical assistance and financing linked to these transactions. Covered products are often identified by their customs classification, or by their relation to a particular sector, project, use or end user. Again you don’t need to know everything, but you should know the kind of products and services your business provides and their major applications. This will help you identify your exposure when sanctions are imposed. The type of products or services targeted by sanctions varies from country to country. Where once sanctions would focus on products or technologies of a military or dual-use nature (meaning they can be used for both commercial and military or other sensitive applications), sanctions have now become more diverse and often include energy or infrastructure-related products and services. This is particularly the case in relation to sanctions on Russia and Iran.

What to do
One simple, practical step is to maintain an up-to-date list of potentially relevant targeted products and services against which you can screen your portfolio. Given adequate time and resources, in-house legal counsel and product experts or engineers can work together efficiently to create such a list. If the product-related sanctions apply only to certain uses of the product, you should ensure that your contract documentation with your business partners contains information or representations relating to the applicable rules and the intended use of the product.

Employees

Need to know
Your employees could create exposure to sanctions in one of two ways. First, your employees could be subject to additional sanctions law obligations due to their nationality or residence. US nationals for instance are bound by US sanctions wherever they are operating. US sanctions are often stricter than those imposed in other jurisdictions. Second, your employees could personally be targeted, for example by being added to the US Specially Designated Nationals (SDN) list, which could, among other things, stop you from paying their wages or providing other benefits, and stop US persons from being able to have any dealings with them.

What to do
To help manage your employee risk, you can: adopt an internal policy for all US persons and other nationals/residents of countries with particularly strict sanctions laws.



Before sanctions

(continued)

What should I know about my business partners?

As an officer or director of your company, you should know your business as best you can, and this should extend to knowing your business partners. These can be your vendors, service providers, sales agents, brokers, distributors or any other person involved in your business, including your customers.

You will need to know if your business partners are targeted by sanctions. If they are, this may affect your ability to continue doing business with them. If you have evidence that a transaction may indirectly benefit a target of sanctions (whether an entity or person) because they are the end-user of your product, be prepared to verify this evidence and, if necessary, to stop the transaction. It can help to screen your business partners and know their approach (if any) to sanctions compliance when acting on your behalf.



Before sanctions (continued)

Is it only the regulators I need to worry about?

Clients are often surprised to find that the banks, insurance companies and other financial institutions they rely on have sanctions compliance policy requirements that go above and beyond what the law requires. Companies based outside the US increasingly must expend time and management resources to respond to due diligence queries from banks and investors relating to even quite limited, and perfectly legal, business that they have with countries targeted by sanctions.

What are the concerns?

Banks and insurance companies have been penalised in sanctions-related enforcement actions. In particular, US federal and state authorities have imposed very large penalties on non-US banks. As a result, most large US and non-US banks have a very low tolerance for sanctions compliance risk. In a sense, financial institutions police the sanctions compliance of the companies they lend to and advise, to make sure they have no risk of being liable for financing or ‘facilitating’ business with sanctioned countries or persons.

Understanding US sanctions

Many international banks and insurance companies take a ‘deemed US person’ approach to compliance. This means it is their policy that all of their US and non-US affiliates comply with US sanctions as if they were US persons. Because of this, it is important that even non-US companies understand the scope of US sanctions, when engaging in financings, capital markets transactions, trade finance or other transactions involving a major international bank, even if the company is not required to comply with US sanctions.

This doesn’t mean non-US companies must comply with US sanctions when the sanctions are not applicable to them – rather, it’s a way to be prepared for and to understand their banks’ and insurance companies’ concerns.

Remaining compliant with sanctions

It is market practice for financing agreements to require sanctions-related representations, warranties and covenants. These cover banks’ concerns that they do not finance or ‘facilitate’ (assist) business with sanctioned persons or countries or business that would otherwise be prohibited under sanctions laws. Banks often seek assurances that a company they finance or advise complies with, and has not violated, the sanctions applicable to that company.

What to do when bank policies make business difficult

Highly restrictive bank sanctions compliance policies can create difficulties for companies doing authorised or exempt business with sanctioned countries. It can be possible to work closely with the bank or insurance company to resolve these policy issues, where there is flexibility in the policy and an understanding that no sanctions laws are being violated. In some cases, seeking guidance or formal approval from a relevant government regulator may help.

In other cases, in an example of the general trend of bank ‘de-risking’, the reality is that the potential risk or compliance cost for the bank or insurance company may make certain types of business transactions unpalatable.



Before sanctions (continued)

How can I stay on top of changing sanctions?

It's vital that you have systems in place to monitor developments in sanctions so you are kept informed when new or expanded sanctions are introduced.

How can I keep on top of sanctions when they change so frequently?

There are online resources that will make this job easier. It's possible, for example, to register online for sanctions alerts from HM Treasury, while the Export Control Organisation – part of the UK Department of Business Innovation and Skills (BIS) – routinely publishes notices to exporters when there are changes to export controls. Knowing when sanctions change is essential, but it's equally important you understand how those changes affect your business. You should put in place systems to monitor the extent to which the products and/or services you provide (or propose to provide) may be prohibited or restricted if provided to sanctioned jurisdictions or persons.

If I've done all my checks, am I protected?

The extent to which you must know your business and follow its developments against the background of sanctions will vary between jurisdictions and according to the size and type of business. As a general remark, several jurisdictions, including the EU, support a risk-based approach to sanctions which allows you to scrutinise your business according to the sanctions risk of the particular business area. This means that you should know and check your business areas with a high risk potential more closely than those with a lower risk potential.

The importance of appropriate due diligence cannot be overstated, particularly in view of the due diligence defence that is available under EU/UK sanctions. Under most EU sanctions, you will not be held liable if you did not know or had no reasonable cause to suspect that your actions in your business area have caused a breach. This limited liability means you don't need to follow each and every strand of your business right to the bottom. However, if you have concrete indications that sanctions could be violated or that your business could be affected by the imposition of particular sanctions, you must verify or remove them, in particular if you do business with sanctioned countries.

My business is in financial services. Are there any specific requirements I need to be aware of?

Businesses in the financial services sector should implement systems that ensure they comply with reporting obligations under various sanctions regimes.

Under EU sanctions, for example, financial institutions have to immediately supply EU member state authorities with any information that would help compliance with the sanctions measures.



Before sanctions (continued)

Should I change my transaction strategy?

Can I use warranties or undertakings in my contracts?

Yes. Many banks and companies carry out sanctions due diligence on other parties before entering into contracts or agreements with them. Some companies rely on commercial screening databases to check on counterparties before entering relationships. Alongside any due diligence that is possible given the time and information available, you can reduce your sanctions compliance risk by asking each of your counterparties for representations and warranties that it:

› is not sanctioned or owned by sanctioned persons;

› has not breached sanctions; and

› will make sure the proceeds of the transaction are not used to benefit any sanctioned person.

These clauses generally apply to the counterparty’s affiliates, officers and directors.

The complexity and restrictiveness of the clauses can be adjusted to reflect the level of sanctions risk and your risk appetite, and are often open to negotiation.

Are there ways to stop economic resources from reaching sanctioned persons?

Potentially, again via undertakings. If funds or economic resources are made available to a counterparty, for example in a capital-raising deal or to buy an asset, the bank or buyer may want an undertaking that the funds will not be used to fund deals with, or invest in, sanctioned persons or territories.

Can I use contracts to guard against the export of sensitive items?

Again, yes. Companies can use contractual language to address risks related to exporting or distributing sensitive items, for example through warranties that counterparties have got the required export licences and undertakings that items won’t be distributed to prohibited jurisdictions. If the clauses are well drafted and supported by a factual record suggesting there was no reason for you to think they were breached, you can use this to build a defence if the counterparty does in fact commit a trade controls violation involving you or your products.

What about M&A deals and investments?

You can use contractual language to address potential legacy liabilities for sanctions violations and the reputational risk of being associated with sanctioned activities.

If your acquisition or merger target is known to have sanctioned persons holding ownership interests or receiving compensation, you can ask for undertakings that the deal will not make economic resources available to the sanctioned persons – for example by paying dividends or salaries using funds derived from the deal.

Also, if the target has business or operations in broadly embargoed countries, under US law it may be necessary to require termination of such business prior to the closing of the acquisition or merger. Any such moves must be made with care and expert advice, as US persons are generally prohibited from assisting or approving transactions in certain embargoed countries, including in connection with a wind-down. In addition, the wind-down of a business in a sanctioned country may raise issues under the sanctions blocking laws in place in the EU, Canada and elsewhere.

Many deals present other sanctions challenges, and may need bespoke provisions to address these risks. For example, sanctions may prevent the transfer of intellectual property rights to a purchaser where sanctions impose restrictions on paying or communicating with local IP registries. It may be possible to mitigate this risk contractually, including through the grant of an exclusive licence pending the IP transfer. Problems with royalty payments and enforcement can also arise if IP rights – including brands and technology – are licensed to or from a business in a sanctioned country.



Before sanctions (continued)

Can I draft contracts that will help if sanctions are imposed?

Sanctions can change very quickly. New persons are designated nearly every day, and sanctions may be lifted or relaxed as the relevant foreign policy goals are achieved. To account for this, contracts often contain clauses related to sanctions.

Sanctions clauses are very common in large financings, capital markets transactions, acquisitions and investments. Increasingly often they are also used in agreements related to the sale of goods or services. Often simple ‘boilerplate’ sanctions clauses are dropped into the agreement, which may provide limited benefit. With a better model clause and a little tailoring for the context, clauses will provide much greater benefit as they will be flexible enough to anticipate any changes in sanctions.

In addition, when entering into agreements with parties that are not sanctioned but are located in countries or sectors with a higher sanctions risk, language can be included that anticipates the counterparty becoming sanctioned after it enters into the contract. For example, force majeure language can specifically address sanctions risk.

Can I terminate an agreement with a sanctioned person?

In some jurisdictions (particularly the EU) a contract may be rendered unenforceable in that jurisdiction’s courts if performing it would be prohibited by sanctions.

At the same time, the sanctions may make it difficult to terminate the agreement with the sanctioned person.

US

US sanctions prevent any dealing with a sanctioned counterpart – which includes terminating an agreement – without a license from the US Treasury’s Office of Foreign Assets Conrtol (OFAC).

Around the world

In other jurisdictions it may be possible to terminate an agreement with a sanctioned person as long as they don’t benefit economically as a result, such as by extinguishing an obligation or debt.



During sanctions

Do sanctions apply to me?

Sanctions are a tool favoured by many governments to address foreign policy and national security issues like terrorism, weapons of mass destruction, drug trafficking, human rights abuses and national sovereignty. Most sanctions seek to achieve governmental goals by shaping the behaviour of individuals and private companies.

With the speed that international events and crises can escalate, sanctions are constantly changing, which means businesses must stay abreast of sanctions to identify new risks, as well as new opportunities that may arise when sanctions are relaxed or lifted.

The EU – like the UN Security Council whose binding resolutions it implements – has in recent years used arms embargoes, economic and financial restrictions. US sanctions similarly include asset freezes, export controls, and sector-specific limitations, for example restrictions on investment, financing or financial services to certain industries in certain countries.

EU sanctions – scope of application

EU sanctions apply to all EU nationals, including entities incorporated or constituted under the law of an EU member state – regardless of where they are doing business. They also apply to all business done in whole or in part within EU territory, including its airspace and on board any aircraft or vessel under the jurisdiction of an EU member state. For these sanctions to apply, it is sufficient that an EU national is involved or that the parties partially act within the EU.

US sanctions – scope of application

US sanctions apply to US persons – that is, any US citizen (including dual nationals), permanent resident (green card holders), any entity formed under US law, any person in the US or any person taking or causing action within the US. US citizens and permanent residents are required to comply wherever in the world they are. US sanctions also apply to non-US persons where there is a sufficient US nexus – for example, sourcing goods from the US to send them to a sanctioned country or person.

In relation to Cuba and Iran, US sanctions also generally apply to non-US entities majority owned or controlled by US persons.



During sanctions (continued)

What transactions are prohibited under sanctions?

Economic and financial sanctions

Economic and financial sanctions often can include:

- › export and/or import bans (trade sanctions that may apply to all trade with a specific country or territory, or to specific products such as oil, timber or diamonds);
- › bans on specific services (brokering, financial services, technical assistance);
- › bans on investment, payments and capital movements;
- › prohibitions on capital raising for targeted entities;
- › arms embargoes, banning the export of weapons and related materials, technologies and services; and
- › the withdrawal of tariff preferences or other trade related restrictions.

The EU and US also impose so-called smart financial sanctions, which target specific persons, groups and entities responsible for objectionable policies or behaviour. These sanctions include an obligation to freeze all funds and economic resources of the targets, as well as a ban under EU law on making funds or economic resources available to the targets and a broad prohibition under US law on any transactions or dealings involving the targets. In addition, US economic sanctions ban most transactions or dealings with the governments of Cuba, Iran, Sudan and Syria, their agents and entities they own or control, or any persons located within or doing business from these countries.

Export controls and arms embargoes

The EU, its member states and the US all impose export controls on trade in restricted goods or technology, including arms and military materials; software that can be used for commercial or military encryption; and other dual-use items that can be used both in commercial applications and in weapons of mass destruction or other sensitive applications. Export controls also apply to restricted items and services for use in Russian deepwater, Arctic offshore and shale oil exploration and production.

Exceptions under EU sanctions

Most sanctions programs include exemptions to allow goods or services to be put to humanitarian or protective use, building programmes and/or crisis management, or in official UN or governmental activities. In the EU, these exemptions are typically subject to prior approval by or notification to a competent authority.

EU sanctions often allow an exemption for contracts concluded before the entry into force of the respective sanctions. By contrast, US sanctions generally do not allow such a grace period.

As sanctions under EU law must be in line with international law and human rights and fundamental freedoms, sanctions targeting individuals have exemptions to take account of their basic human needs, for example releasing sufficient funds for their basic living expenses from the asset freeze. US sanctions do not contain any general allowances of this type for targeted individuals, rather such exceptions must be sought on a case-by-case basis from the US government.

Exceptions under US sanctions

Each US sanctions programme has its own general authorising activities that would otherwise be banned under the sanctions. With certain exceptions, the US government authorises a large volume of US exports of food, medicine and medical devices to Cuba, Iran and Sudan.

Certain non-commercial activities are also exempt: family remittances, donations of agricultural or medical goods, personal communications not involving the transfer of value, and personal communications software available for free over the internet.

Imports or exports of information are generally exempt, and related payments and other transactions ordinarily incident to such imports and exports may also be exempt. US sanctions regulations contain complex provisions in this area. Generally not exempt are information subject to export controls, marketing and business consulting services, and information not yet in existence (commissioning an article or book).



During sanctions (continued)

Should I pull out of sanctioned markets?

Trade restrictions are historically aimed at debarring specific individuals or entities from any commercial activity, or prohibiting the delivery of certain goods or services. For many years, sanctions have been extended to cover certain business sectors including oil and gas exploration, financial services, transport and telecommunications.

To decide how much you should withdraw from sanctiontargeted markets, you'll need to consider the broader risk picture and outlook for future changes in sanctions.

Withdrawing from a market can affect your activities in a number of ways:

- › **Operationally** through the shutdown of factories or stores, and a reduction in your headcount. It may also have an impact on your group businesses in other markets. If sanctions are introduced they may prevent you from offering your products or services – or at least a certain spectrum of your product line – in a particular market. A comprehensive ban may require you to completely withdraw from the market, but if a partial ban is introduced (i.e. one that affects only certain products) it may still be possible to remain in the market from a legal and economic perspective.
- › **Legally** through the termination of contracts, which may give rise to a series of disputes with existing customers, and corporate reorganisation measures.
- › **Technically** through a reduction of capacity and stock and a shift of raw materials and suppliers.
- › **Financially** through a reduction of your revenue streams and/or a restructuring of your debt and credit lines (which may reduce the availability of financing or make it more expensive). Being active in a sanctions-targeted market will also require you to set up an internal sanctionscompliance system that will trigger additional costs. Your insurance premiums may also rise. Payment streams into or out of the sanctioned market may also require a permit and banks may refuse to process payments, even if they are legally permitted.



During sanctions (continued)

Can I get out of contracts with sanctioned persons?

When sanctions are imposed they can interfere with existing contracts. If your counterparty becomes targeted by sanctions there are many things to take into account.

- › Consider the extent to which you need to stop or suspend performance of your obligations under the contract. You may need to consider carefully if there are grandfathering provisions in the sanctions themselves, and/or authorisations available from the competent authorities.
- › Consider whether you must freeze and report to a regulator any funds or other assets of the sanctioned counterparty that are in your possession or control. If the relevant sanctions targeting the counterparty include an asset freezing requirement (called ‘blocking’ under US sanctions) you may have immediate and broad obligations of this type.
- › Depending on the facts, a doctrine of ‘frustration’ could apply. For example, under English law, this is the case when the contract cannot be performed because the circumstances make it a radically different thing to what the parties intended. To determine whether a contract is frustrated, the English courts consider many factors. These include the parties’ knowledge, expectations and assumptions at the time of contract, as well as the nature of the supervening event and the parties’ reasonable views as to whether the contract could be performed in future. Similar legal concepts exist in a number of other jurisdictions.

- › It is not uncommon for a contract to include a force majeure clause designed to allow you or your counterparty to cancel the contract – or to be excused temporarily or permanently from performing it – if specified events, or events beyond one or both parties’ control, arise. Such clauses are construed differently by the courts of different jurisdictions. For example, English courts tend to construe force majeure clauses strictly, and it is advisable to expressly refer to sanctions in these clauses if you intend them to be covered. English courts will generally expect parties seeking to rely on a force majeure clause to show that they have taken all reasonable steps to avoid its operation or mitigate its results (which, depending on the facts, could include seeking available authorisations from the competent authorities).
- › The legal rules (including associated case law) that govern when a party can rely on frustration, illegality or a force majeure clause are complex. Each case will need to be assessed carefully on its facts.

US sanctions considerations

When winding up business with sanctioned persons, or shutting down operations in sanctioned countries, it’s important to understand the requirements of US sanctions.

- › No US parent company or investor should be involved (or even appear to be involved) in the termination process – particularly any negotiations or other direct dealings with sanctioned persons – without express authorisation from the US government.
- › Any involvement could constitute a facilitation of the subsidiary’s or acquisition target’s dealings (even if only to wind up existing business) with sanctioned persons or countries, or a prohibited provision of advice or services that indirectly benefit an OFAC-sanctioned person or country.
- › If there is substantial risk of actual or perceived US person involvement in the divestment, some companies will seek a specific licence from OFAC to authorise US parent companies or other US persons to help make decisions, plan and implement the process.
- › OFAC typically takes a long time to decide on a licence application, and the licence may contain limitations or exclusions that make it difficult to implement, or uncommercial.
- › A practical rule of thumb: terminating business with sanctioned persons or in sanctioned countries always takes longer and is more complicated than expected.



During sanctions (continued)

How can I protect my assets in a sanctioned country?

Sanctions have just been announced against a country where you do business or own assets. What should you do?

- › **Prepare in advance** – Sanctions can often be anticipated before they are imposed. Contingency planning can help you react quickly to events. Consider conducting advance due diligence of your operations in higher risk jurisdictions to determine the ownership, control and management structure of local business partners, particularly those with political connections. [See What should I know about my own business? for more details.]
- › **Understand the new sanctions** – Sanctions rules are often complex. It is important to determine quickly which elements of your business are affected, and what changes you need to make to your operations, including a potential withdrawal. [See Do sanctions apply to me? and Should I pull out of sanctioned markets? for more details.]

- › **Engage with your counterparties** – You may have legal obligations that you are no longer able to fulfil, as to do so would be in breach of the new sanctions rules. You will need to engage with your contractual counterparties and local business partners to avoid potential disputes, relying on contractual and applicable law defences where available. [See Can I get out of contracts with sanctioned persons? for more details.]

- › **Speak to your regulators** – Regulators might be willing to provide a licence that allows you to continue certain activities or allows you to take the necessary steps to wind down your business and withdraw your assets. You may also need to show that you engaged with your regulators if you want to rely on defences such as force majeure in disputes with counterparties.

- › **Update your internal policies** – Your business needs to know what actions are forbidden under the new rules. Having robust compliance policies can also help avoid penalties in the event there are inadvertent breaches. You may have to exclude certain employees, such as US or EU nationals, from certain activities. You may also have to exclude certain holding companies, including those in the US, EU or certain offshore jurisdictions. Be careful you are not simply circumventing the sanctions – this could be a breach itself.

- › **Engage local counsel** – You will likely need someone to advise you on the situation on the ground and to avoid breaches of local law.

- › **Speak to your banks and insurers** – Even if certain activities are not in breach of sanctions your banks or insurers may be unable or unwilling to provide the support you need. It is helpful to start a dialogue with them as early as possible and consider measures such as ring-fencing of funds.

- › **Protect your reputation** – Breaching sanctions can cause major reputational as well as financial damage. However, being overly cautious and pulling out of business unnecessarily can also have a negative impact, so you need to balance these concerns.



During sanctions (continued)

What should I do if I’m worried about a breach?

The following are 20 steps you can take to design and implement an effective internal investigation of sanctions issues.

Assess your regulatory exposure

1. Consider your risk in relation to your products, services and any sectors that have been targeted by sanctions; your work in, or dealings with, countries or individuals subject to sanctions; and your handling of products or currencies.
2. Work out which regulators are likely to claim jurisdiction and the scope of their powers. Things to consider include where a company is registered or has a physical presence; where the conduct took place or was directed from; the nationality and location of the employees involved in the conduct or decision-making; and where the products or currencies travelled to, through or from.
3. You should also consider how regulators share information, if certain regulators are likely to take the lead in a multi-jurisdictional investigation, and whether other authorities are likely to launch a ‘me too’ investigation. Tackling an issue in isolation may have unintended consequences elsewhere.

Consider what’s at stake

4. You should identify the possible consequences of the investigation, including the potential for criminal and civil penalties; the effect on your reputation; the likelihood of increased scrutiny from other regulators (for example into competing obligations such as conflict between US sanctions and anti-boycott and antidiscrimination laws in Europe and other countries, such as Canada); and any burdensome settlement terms such as the use of prolonged monitorships.

Apply a proper scope

5. You should scale your investigation to the portion of your business that appears to be affected; the level of suspicion of a breach of sanctions; the magnitude of the potential wrongdoing; and the legal standards that apply. A dynamic, staged approach (where the scope is initially targeted then expanded as necessary) often yields a right-sized investigation.

Empower a central team to co-ordinate the investigation and PR messaging

6. It’s important to build a central response team to co-ordinate the investigations. For multijurisdictional investigations, a single control point fosters consistent factual and legal analysis; consideration of differences in applicable laws and regulations; and preservation of privilege.
7. A centralised approach should also be used for public relations and messaging. Appoint a primary point of contact for press inquiries. In turn, instruct the PR contact to work with legal counsel for proper vetting of public statements.
8. Ideally, responsibility for an investigation should rest with individuals other than the line managers responsible for the operations at issue. If line managers have to conduct the investigation, it’s vital to engage support from an independent party (eg external counsel or senior internal compliance).
9. The seriousness and scope of the potential compliance issue should inform who leads the investigation. In some instances, a company’s management board or audit committee should be in charge.

10. Bigger investigations, particularly international ones, can result in disruptive or non-co-operative behaviour from your employees. Internal investigations are aided by high-level support for the investigation and the vesting of proper authority in those taking the lead.

Consider who should receive legal representation – and how

11. In many jurisdictions, the involvement of internal counsel is not enough to extend legal privilege to documents created during an investigation. It may be advisable to involve external counsel as early as possible.
12. Investigations can create diverging legal interests between a company and its employees when employee conduct is at issue. Consider whether independent legal representation is needed, whether national law imposes any relevant restrictions, and review

Assess whether employee discipline is appropriate/permitted

13. It’s important to assess whether employees can or should be suspended or dismissed while an investigation is under way.

Work out how to preserve evidence and manage data efficiently

14. Notify the relevant employees of any document preservation requirements. Employees should avoid creating new documents – particularly unprivileged ones – concerning the matter.

15. Where possible, any information collected should be consolidated in a single database for efficient review and keyword searching. However, server location should be considered as it may have implications for whether a regulator has jurisdictional access to evidence.

Assess how to preserve legal privilege and comply with data protection laws

16. In order to prevent inadvertent waiver, it’s important to account for differences in the concept of privilege across jurisdictions.
17. Due to some jurisdictions’ comprehensive data protection systems (eg the EU’s Data Protection Directive), you may need to anonymise data or object to certain data requests.

Consider issues relating to self-reporting, public disclosure and settlement

18. Self-disclosure of an undetected violation can mitigate a penalty and allow you to control how the issue is portrayed in the press and public filings. You should assume that self-reporting to one regulator will result in information-sharing with others.
19. Consider the disclosures you need to make to meet capital markets requirements, and the timing and level of detail required by each exchange.
20. It is often desirable to resolve an issue through one global settlement across regulators, particularly where a sanctions issue coincides with investigation of another regime (eg export controls, anti-money laundering, or anti-bribery and corruption).



During sanctions (continued)

What should I do if sanctions are being imposed during negotiations?

What you should do...

Assess whether your deal is still possible the new sanctions may not apply to you.

Details – You need to consider the jurisdictional application of the relevant sanctions. For example, if your counterparty becomes designated under US sanctions, they may not apply provided there is no involvement of US persons, payments in US dollars or other US jurisdictional nexus. You'll need to ensure that no US citizen or permanent resident (green card holder) is involved in approving or otherwise facilitating any dealings with the US-sanctioned counterparty. Any such individuals acting as directors or senior officers may need to recuse themselves. You should also consider the reputational risks that arise from dealing with a sanctioned person, even if the sanctions are not directly applicable.

Consider whether the new sanctions affect the value of the deal.

If performance under a contract becomes prohibited under sanctions, it may be difficult to enforce it or to unwind the transaction, and any pre-payments or deposits may have to be frozen (or 'blocked' to use the US term). Even if an agreement or transaction can be unwound without violations, it may not be possible to receive payment from a sanctioned counterparty without an authorisation from the relevant authorities.

Consider whether further sanctions are likely to be imposed.

In some circumstances, a counterparty may be targeted under limited sanctions that do not generally restrict commercial dealings. However, the parties to the agreement may be concerned that more restrictive sanctions might be imposed in the future. In such circumstances, it may be possible to include provisions in contracts for 'divorce proceedings' that would take effect automatically to unwind the deal in the event of further sanctions.

Consider what protections you can add into the deal to help mitigate the risks.

We have also seen a 'currency toggle' provision that would permit the parties to an agreement to accept payment in an alternative currency should payment in the original currency be restricted or prohibited by sanctions. However, it is important to ensure that any decision to change currency under such a provision doesn't violate the relevant sanctions. For example, US persons may be prohibited from participating in a decision to change currency from US dollars for a payment from or to a US-sanctioned person, as such action could constitute circumvention of US sanctions.

...and what you shouldn't do

Be careful if you renegotiate your deal, to ensure this could not be construed as trying to circumvent the sanctions.

Details – In general, actions taken in anticipation of possible future sanctions are not prohibited, but once sanctions are in place persons required to comply with the sanctions must have no involvement in steps to circumvent them, including any approval or facilitation of the renegotiation, or any delegation of such actions to another person who is not subject to the relevant sanctions.



During sanctions (continued)

What are capital market sanctions?

Sanctions fall into two categories:

- › limited sanctions, which impose restrictions on specific sectors or types of transactions; and
- › broad embargoes, which prohibit most dealings with targeted persons or involving targeted countries.

Both types of sanctions may target designated natural or legal persons. Limited sanctions often only include specific restrictions within a targeted sector, and they do not cover all dealings with targeted people or countries. The object and purpose of the sanctions determines what is prohibited and what is not.

Capital markets sanctions are a type of limited sanctions that aim to restrict the targeted company’s access to certain capital or debt markets. Transactions related to the capital markets are permitted if they do not involve new securities or debt of a targeted company – for example, a targeted entity may act as an underwriter of securities issued by a non-sanctioned issuer or as a lender to a non-sanctioned borrower. Other financial businesses unrelated to the capital markets are unlikely to be affected unless they involve a prohibited extension of credit.

What do they do?

Broadly, the object and purpose is a good, rough guide to interpreting the scope of limited sanctions. But because some limited sanctions, like capital markets sanctions, are new, their scope is not always clear, and even competent national authorities within the EU do not necessarily share the same understanding of the scope of these sanctions.

Limited sanctions target individuals and entities for a variety of reasons; however, they often follow general rules that are similar to those that apply to broad embargoes. For example, US capital markets and other limited sanctions apply to virtually all US-dollar transactions. Also, like US blocking (asset freeze) sanctions, US capital markets sanctions apply not just to listed companies but any entities in which a listed company directly or indirectly has a 50 per cent or greater ownership interest.

What is not prohibited?

Capital markets sanctions do not affect credits, loans or other financing contracts concluded before the sanctions entered into force. But these contracts may be subject to limitations. For example, if there are any terms of the loan or contract subject to negotiation or agreement by the parties after the effective date of the sanctions, it may constitute a prohibited new extension of credit. However, some exercise of discretionary terms, such as early termination, may be permitted if it is solely to the detriment of the targeted company.

As capital markets sanctions aim to prevent long-term financing, short-term credits, loans, etc (not exceeding a certain maturity) are not prohibited by limited sanctions.

In the EU, trade financing and emergency funding to targeted legal persons is generally not prohibited.

And EU capital markets sanctions do not apply to legal persons, entities or bodies that are established within the EU, even if a targeted person owns the entity or body, provided the entity or body is not acting on behalf of or at the direction of a non-EU targeted person.

What is prohibited?

It is generally prohibited to provide mid- or long-term financing to targeted persons.

Capital markets sanctions measures ban granting new credits or loans to targeted persons with a maturity that exceeds 30 to 90 days.

Capital markets sanctions may ban buying, selling, providing investment services or otherwise dealing with specific new debt and equity instruments, such as transferable securities and money markets instruments with a maturity similar to the above.



After sanctions (continued)

What should my strategy be?

You should have a back-up plan in case sanctions are re-imposed – just because sanctions have been lifted doesn’t mean they are gone for good. For example, while changes in the UN, EU and US sanctions against Iran following implementation of the landmark nuclear deal are significant, challenges remain for companies looking to do business in Iran. Ensuring that transactions are compliant with the continuing sanctions and export controls is critical, as is an understanding that sanctions can ‘snap back’ into place if Iran fails to meet its commitments under the Joint Comprehensive Plan of Action (JCPOA). Companies should factor this into the consideration and structuring of any investment.

Resume business with caution

Even if sanctions are re-imposed, you can reduce your risk by always keeping your exit strategy in mind. It’s never possible to know in what form sanctions might be re-imposed, so keep a close eye on the situation and make sure your compliance teams are informed of your dealings in sanctioned countries.

After sanctions (continued)

Where are the risks in a post-sanctions environment?

The lifting of sanctions will present a mixture of risks and opportunities.

Investment opportunities post-sanctions tend to arise in emerging markets, where you will need to analyse sanctions risk alongside anti-corruption and other regulatory and compliance issues.

Engaging in thoughtful due diligence at the outset of your investment will help you avoid pitfalls further down the line.

Risk	Comments
Sanctions	<p>Broad sanctions programmes are not lifted all at once, but are instead removed in stages over a period of months or even years (and may, as with the Iran sanctions, be subject to reinstatement if certain commitments by the sanctioned, or previously sanctioned, country are not met). During this time, a thorough understanding of what is authorised and what remains prohibited can help mitigate the risk and unlock opportunities presented to early movers in an opening market.</p> <p>When entering or re-entering any market, the first focus must be on your proposed business partners. You should conduct sufficient diligence on them, particularly to learn if they have ties to sanctioned persons or formerly sanctioned persons. This diligence is key to understand whether your dealings with them might threaten your reputation.</p>
Human rights	<p>The sanctions regimes can be imposed because of human rights concerns which can remain even when sanctions are lifted. Even if it is legal to do so, there may be reputational concerns with engaging with certain individuals or groups.</p>
Bribery and corruption	<p>The nature and degree of corruption risk you encounter in emerging markets will vary greatly from country to country, from a desk clerk demanding a tip to a government minister asking for kickbacks. Legislation such as the US Foreign Corrupt Practices Act and UK Bribery Act give authorities the right to prosecute those bound by it, wherever their alleged misconduct takes place.</p>
Intellectual property	<p>It’s vital to protect your brands, technology and know-how, but IP laws in emerging markets are often underdeveloped. Some jurisdictions are beset by bureaucracy and give priority to the first person to use IP. On the positive side, US and some other sanctions generally allow for IP registrations and filings, so in a country where sanctions are being lifted generally it is possible to move quickly to protect your IP.</p>
Competition law	<p>The number of competition regimes around the world is growing, and authorities are using more and more sophisticated investigation techniques. Enforcement in emerging markets can be aggressive and target everything from cartels to softer behaviour such as joint-selling.</p>

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