Swedish Trade Compliance Association

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Agenda

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Public International Law Principles on Extraterritoriality

Principles on Extraterritoriality

When a state attempts to make, apply and enforce rules of conduct in respect of events outside its own territory, they are only permitted to do so when acting under one of the key 5 principles:

1. **Active Nationality Principle**
   - A State may exercise jurisdiction in respect of its own nationals abroad, including not only natural persons but also companies, ships and aircraft that have its nationality.
   - This principle allows states to prosecute its nationals for crimes committed outside its territory, even if the crime is not considered a violation of its own laws.
   - For example, if a German national commits a crime in Kenya, Germany can exercise jurisdiction over them, even though the crime may not be a violation of German law.
2. **Passive Personality Principle**
   - A State may exercise jurisdiction in respect of conduct abroad which injures its own nationals.
   - This has traditionally been the most controversial principle, with many common law countries originally objecting to its application, but it is now commonly accepted.
   - While the principle was initially more commonly used by civil law states, its application has broadened over time, particularly in the context of terrorism and crimes against nationals abroad.

Principles on Extraterritoriality (Cont.)

3. Protective Principle

- A State may exercise jurisdiction in respect of persons, property or events abroad that may constitute a threat to its essential interests, including acts against national security, such as terrorist acts, counterfeiting currency and forging passports.
- Although the validity of this principle is not contested it provides a rather uncertain basis for the exercise of extraterritorial jurisdiction because the conditions under which it may be relied upon are ill-defined.

4. Universality Principle

- A State may exercise jurisdiction in respect of certain serious crimes irrespective of the location of the crime and irrespective of the nationality of the perpetrator or the victim.
- The principle is applicable only to certain crimes under international law that have been made subject to universal jurisdiction either by a multilateral treaty or under customary international law, such as genocide, war crimes and torture.
- Unlike the protective principle the interests protected are not those of the prosecuting State but those of the international community as a whole.

5. Effects Principle

- A State may exercise jurisdiction when foreign conduct produces substantial effects on its territory.
- The effects principle tends to be invoked in support of the exercise of extraterritorial jurisdiction in commercial rather than criminal cases.

EU Blocking Regulation

EU Blocking Regulations

Origin

- Council Regulation (EC) No. 2271/96 (the "EU Blocking Regulation") was introduced to neutralise the extraterritorial effect of U.S. sanctions against (at the time) Cuba, Iran and Libya on EU persons.
- Since its introduction in 1996, the EU Blocking Regulation had seen little enforcement - became more of a political statement rather than a law with teeth (e.g., BAWAG case).
- Many EU Member States did not even have (administrative/criminal) penalties for non-compliance with the EU Blocking Regulation on the books.

Reform

- This changed in 2018, when, upon pulling out of the Iran nuclear deal, the Trump Administration announced it would re-impose sanctions on Iran. In this context, the EU re-considered the EU Blocking Regulation, and its extra-territorial effect, as a means to counter these new sanctions.
- Commission Implementing Regulation (EU) 2018/1101 allows EU companies to request an authorisation to fully or partially comply with U.S. requirements or prohibitions in circumstances where non-compliance would seriously damage their interests or the interests of the European Union.

EU Blocking Regulations restrictions at a glance…

Article 2

This imposes a notification requirement if an EU person's economic and/or financial interests are affected, directly or indirectly, by the blocked U.S. laws.

Article 4

This prevents the recognition and enforceability in the EU of U.S. court judgments and administrative authority decisions giving effect to the blocked U.S. laws.

Article 5

This provides that no EU person shall comply with U.S. sanctions against Cuba or Iran "*whether directly or through a subsidiary or other intermediary person, actively or by deliberate omission, with any requirement or prohibition, including requests of foreign courts, based on or resulting, directly or indirectly, from the laws specified in the Annex or from actions based thereon or resulting therefrom*" unless a license permitting such compliance has been obtained from the Commission.

Article 6

This sets out that any EU person "*shall be entitled to recover any damages, including legal costs, caused to that person by the application of the laws specified in the Annex or by actions based thereon or resulting therefrom*".

Bank Melli Iran v Telekom Deutschland GmbH Case C-124/20

- *EU Blocking Regulation*
- *Key Conclusions*
- *Practical Considerations*

Bank Melli Iran v Telekom Deutschland GmbH

- After the U.S. reinstated its Iran sanctions in 2018, Bank Melli Iran (the "Bank") again became a U.S. sanctioned party (Specially Designated National or SDN).
- The Bank had entered into a contract with Telekom Deutschland GmbH (the "Company") for the provision of its telecommunications services. The Company terminated this contract (and its services), without reason, 11 days after the Bank was sanctioned by the U.S. on 5 November 2018. The Bank subsequently sued the Company, seeking a court order requiring it to continue providing telecommunications services.
- The case was initially heard before a German court, which deemed the Company's contract termination valid on the basis that, under German law, terminating contracts without justification is permitted at any time after the statutory notice period has passed.
- The Bank appealed to the Hanseatic Higher Regional Court, arguing that the Company's decision to terminate the contract was in breach of the EU Blocking Regulation. The Hanseatic Higher Regional Court referred various questions to the European Court of Justice (the "CJEU") for a preliminary ruling.

Key Conclusions

1. EU persons can be found in breach of the EU Blocking Regulation even if they voluntarily comply with U.S. sanctions and are not subject to any direct orders or enforcement proceedings by U.S. authorities.

2. EU persons terminating contracts with U.S. sanctioned parties are not obliged to disclose the reasons for termination if national law does not compel them to do so. However, if civil proceedings arise from the termination and there is *prima facie* evidence that the terminating party complied with the blocked U.S. sanctions, the burden of proof shifts to that party.

3. Courts can annul the termination of a contract if it is found that such termination was in breach of the EU Blocking Regulation. However, such a decision must be supported by a proportionality test; EU Member State courts must weigh how the invalidation of a termination serves the EU Blocking Regulation's objectives against the EU person's exposure to secondary sanctions and the EU person's ensuing economic losses if they would not be permitted to terminate the contract.

Key Conclusions (cont'd)

4. Many EU Member States (and the UK) have made breaches of the EU Blocking Regulation a criminal offence. However, in the absence of actual enforcement, that risk appears (very) low.
5. The Bank Melli judgment demonstrates that the key risk is contractual:
    - A termination may be invalid.
    - Which leads to a continuation of an agreement.
    - Which puts the EU person in the position of breaching U.S. sanctions, which may pose U.S. enforcement risk.
    - The threat of U.S. enforcement is real, EU enforcement is (currently) not, and the continued contractual exposure can (in most cases) be resolved by compensation.

Practical Considerations

- There is no legal obligation for EU persons to continue doing business with companies subject to U.S. sanctions for purposes of the EU Blocking Regulation
- However, the reasons for terminating contracts with U.S. sanctioned parties will continue to be scrutinised by courts and arbitrators in the EU with the focus being to determine whether a contract was terminated for clear and demonstrable reasons other than for (prohibited) compliance with U.S. sanctions
- EU persons should have in place internal policies governing counterparty relationships, which may incorporate anti-bribery and corruption, commercial, human rights and corporate social responsibility considerations. Termination of relationships with counterparties should be guided by same policies rather than compliance with U.S. sanctions
- Obtaining a license from the Commission to comply with U.S. sanctions targeted by the EU Blocking Regulation is something to consider but is proving to be (at the moment) a cumbersome and lengthy process. Moreover, if this route is pursued, it precludes reliance on internal policies and therefore could be detrimental in the event of civil litigation (particularly if a license is not obtained)

Practical Considerations (cont'd)

Items to consider:

- It is market standard for agreements to include compliance with U.S. sanctions, even in the absence of U.S. jurisdiction over lenders/borrowers or their business.
- Internal policies established at U.S. HQ.
- Other agreements with suppliers may require (unconditional) compliance with U.S. sanctions.
- Compliance with terms & conditions of U.S. General Licenses.
  - Example: U.S. GLs generally do not authorise transactions with SDNs. An internal policy that confirms no business with U.S. SDNs may breach the EU Blocking Regulation. This risk can be mitigated by a general statement that no business shall be done with persons/entities included on a sanctions list (as established by certain relevant jurisdictions – not limited to the U.S.).

Potential impact of third country blocking laws

China and its Anti-Foreign Sanctions Law

China and the Anti-Foreign Sanctions Law ("AFSL")

- China has adopted a mixed model of countermeasure and blocking legislation.
- AFSL Countermeasure criteria:
  - Where a foreign country in violation of international law and basic norms of international relations contains or suppresses China under various pretexts or pursuant to its own laws, adopts ***discriminatory restrictive measures against any Chinese citizen or organization***, China has the right to adopt corresponding countermeasures (**Article 3**).
- AFSL Countermeasure provisions:
  - The State Council may take countermeasures, which include: (1) Denial of entry; (2) asset seizure; (3) attachment or freezing; (4) transaction prohibitions; and (5) any other necessary measures (**Article 6**).
  - Imposes a binding obligation to comply with China's countermeasures (**Articles 11 & 14**).
  - State Council can authorise, suspend, modify or terminate countermeasures based on situational developments, which are subject to official public announcements (**Articles 8 & 9**).
  - Authorises the State Council to take necessary countermeasures against organizations and individuals that endanger China's sovereignty, security or development interests (**Article 15**).
- AFSL Blocking measures:
  - Prohibits any person from assisting in the implementation of foreign sanctions and grants Chinese entities the right to initiate legal proceedings against violators (**Article 12**).

Article 8a and Article 12g of EU Regulation 833/2014

Article 8a EU Regulation 833/2014 - best efforts obligation

- *"Natural and legal persons, entities and bodies shall undertake their best efforts to ensure that any legal person, entity or body established outside the Union that they own or control does not participate in activities that undermine the restrictive measures provided for in this Regulation."*
- 'Best efforts' should be understood as comprising all actions that are suitable and necessary to achieve the result of preventing the undermining of the restrictive measures in EU Regulation 833/2014. Those actions can include, for example, the implementation of appropriate policies, controls and procedures.
- 'Undermine' involves activities "*resulting in an effect that [the] restrictive measures seek to prevent, for example, that a recipient in Russia obtains goods, technology, financing or services of a type that is subject to prohibitions under Regulation (EU) No 833/2014*".
- At the same time, 'best efforts' should be understood as comprising only actions that are feasible for the EU operator in view of its nature, its size and the relevant factual circumstances, in particular the degree of effective control over the legal person, entity or body established outside the Union. Such circumstances include the situation where the EU operator, due to reasons that it did not cause itself, such as the legislation of a third country, is not able to exercise control over a legal person, entity or body that it owns.
- The operator's nature and size reflect various elements such as its market sector, risk profile and turnover, and, for entities, the number of staff. Apart from the degree of effective control over the non-EU operator, the relevant factual circumstances include the compliance resources available to the operator. Such elements should be taken into consideration together. For example, even if an operator is relatively small in size, the fact that it operates in a highly regulated sector with abundant compliance resources means that substantial actions are to be expected.
- The precise scope of best efforts that can be expected from each EU operator will differ on a case-by-case basis.

Article 12g EU Regulation 833/2014 – no “re-export to Russia” clause

- *“When selling, supplying, transferring or exporting to a third country, with the exception of partner countries listed in Annex VIII to this Regulation, goods or technology as listed in Annexes XI, XX and XXXV to this Regulation, common high priority items as listed in Annex XL to this Regulation, or firearms and ammunition as listed in Annex I to Regulation (EU) No 258/2012, exporters shall, as of 20 March 2024, contractually prohibit re-exportation to Russia and re-exportation for use in Russia.”*
- Exporters are also required to ensure that their export/sale/supply/transfer or similar contracts with third-country counterparts contains adequate remedies in the event of a breach of the no “re-export to Russia” clause. These remedies should be reasonably strong and aim to deter non-EU operators from any breaches (e.g., a remedy that allows for EU operators to stop deliveries and to suspend, interrupt or terminate the contract as soon as it becomes aware of a breach).
- Exporters should generally not sell their products to any non-EU operator that is not ready to incorporate a “no re-export to Russia” clause in contracts falling under the scope of Article 12g.
- EU Guidance states that independent from the Article 12g obligation, operators should have in place due diligence frameworks to ensure sanctions compliance and to mitigate against the risk of circumvention.
- The obligation to include a “no re-export to Russia" clause applies to contracts with operators based in any non-EU country, with the exception of the partner countries listed in Annex VIII (United States of America, Japan, United Kingdom, South Korea, Australia, Canada, New Zealand, Norway, Switzerland, Liechtenstein and Iceland).
- While there is no prescribed wording required for the no “re-export to Russia” clause – the EU Guidance provides for a template wording.

Interaction between Article 8a and Article 12g

- ***Do the obligations under Article 8a require EU companies to compel their non-EU subsidiaries to implement no "re-export to Russia" clauses?***
- EU Guidance appears to introduce an extra-territorial element to the relevant sanctions regimes by effectively requiring, for example, subsidiaries located in the United Arab Emirates (UAE) or Singapore that are owned or controlled by EU operators to comply with the relevant EU sanctions against Russia.
- This represent a significant departure from the EU's longstanding position on the non-extraterritoriality of EU sanctions.
- EU Guidance appears to suggest that EU persons will now need to monitor the internal governance processes and procedures of non-EU subsidiaries not subject to EU law for compliance with applicable EU sanctions.
- An EU operator's "degree of effective control" over its non-EU subsidiaries will be a key factor in determining whether actions taken are consistent with "best efforts". The FAQs suggest that non-EU subsidiaries trading restricted goods in Russia are within scope, as this may indicate that the EU operator has not "performed all actions necessary and feasible to prevent the undermining of EU sanctions" by the non-EU subsidiary (see FAQ 9).

Questions?

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