



International Trade & Regulatory ADVISORY ■

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OFAC Issues New Guidance on Entities Owned by Specially Designated Nationals

On August 13, 2014, the Department of the Treasury's Office of Foreign Assets Control (OFAC) issued [new guidance](#) detailing the agency's current thinking on entities owned by persons included on the Specially Designated Nationals (SDN) list. The new guidance was also accompanied by frequently asked questions ([FAQs – see FAQs #398-402](#)) that provide additional commentary on the application of the new OFAC guidelines, which are applicable to OFAC's new Russia sanctions related to the Ukrainian situation.

The new guidance changes past guidance on determining if an entity is an SDN by operation of law. An entity owned 50 percent or more in the aggregate by one or more SDNs is itself considered an SDN whether or not it is on the SDN list. Previously, in the context of the Russian sanctions, OFAC had advised that the ownership interests of SDNs should not be aggregated to evaluate whether an entity was owned 50 percent or more by an SDN.

Now, OFAC has decided that ownership interests of SDNs must be aggregated in terms of a specific SDN's direct and indirect ownership, as well as the collective ownership interest in a given entity by all SDNs. OFAC's FAQs also provide clarity on indirect ownership. Specifically, indirect ownership is ownership of an entity through another blocked entity, i.e., an entity owned 50 percent or more by SDNs. For example, if an SDN has a 10 percent direct ownership in Company A and a 50 percent direct ownership in Company B, then Company B is considered subject to the SDN restrictions. However, if Company B itself owns 40 percent of Company A, then both companies would be covered under OFAC's new guidance, because the SDN's 50 percent direct ownership of Company B results in Company B's 40 percent direct ownership of Company A being deemed a 40 percent indirect ownership of Company A by the SDN. Thus, there is a 40 percent indirect ownership and 10 percent direct ownership in Company A by the SDN.

Additional illustrative examples are provided in OFAC's FAQs:

SDN owns 50 percent of Entity A and 50 percent of Entity B. Entities A and B each own 25 percent of Entity C. Entity C is considered to be blocked. The SDN's 50 percent ownership of Entity A results in a 25 percent indirect ownership of Entity C. Similarly, the SDN's 50 percent ownership of Entity B results in another 25 percent indirect ownership of Entity C, resulting in a 50 percent total ownership of Entity C by the SDN.

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Entity C is also considered to be blocked due to the 50 percent aggregate ownership by Entities A and B, which are themselves blocked entities due to the SDN's 50 percent ownership of each.

SDN owns 50 percent of Entity A and 25 percent of Entity B. Entities A and B each own 25 percent of Entity C. Entity C is not considered to be blocked. Even though the SDN is considered to indirectly own 25 percent of Entity C through its 50 percent ownership of Entity A, Entity B is not 50 percent or more owned by the SDN and, thus, the SDN is not considered to indirectly own any of Entity C through Entity B. The SDN's total ownership (direct and indirect) of Entity C, therefore, does not equal or exceed 50 percent.

OFAC's new FAQs also make it clear that when multiple SDNs own an interest in an entity, such ownership percentages must be aggregated to determine whether the owned entity is to be treated as an SDN. In other words, if two SDNs each have a 25 percent ownership interest in Company Z, then Company Z is deemed blocked even though no single SDN has a 50 percent or greater ownership interest.

It is important to note that the **new OFAC guidance is applicable to all existing relationships** and, as a consequence, previously permissible transactions and dealings are now prohibited. For example, SMP Bank was controlled by two brothers on the SDN list, Arkady and Boris Rotenberg. Neither of the brothers individually had a 50 percent or greater ownership in SMP Bank and, under prior OFAC guidance, SMP Bank was not deemed blocked (OFAC eventually blocked SMP Bank by placing the entity on the SDN list). However, under the new guidance, SMP Bank would be blocked without an explicit SDN listing, provided that the Rotenbergs, or any other SDNs, had an aggregate ownership of 50 percent or more. **Therefore, previous due diligence screens for SDNs may need reexamination to ensure compliance with the new guidance.**

Despite this expansive interpretation by OFAC, the agency made it clear that an SDN by operation of law can arise only from ownership and not from control, i.e., corporate control exercised through less than 50 percent ownership. Furthermore, OFAC states that if an SDN divests a triggering ownership in an entity such that aggregate ownership of the entity by SDNs drops below 50 percent, then that entity is no longer subject to the SDN restrictions. Such divestiture, however, would have to occur entirely outside the United States and not involve U.S. persons.

The new OFAC guidance will clearly require companies to engage in more thorough due diligence in evaluating and monitoring business relationships.

Please direct any questions concerning this matter to either **Tom Crocker** or **Ken Weigel** of Alston & Bird's International Trade & Regulatory Group at, respectively, thomas.crocker@alston.com, 202-239-3318, and ken.weigel@alston.com, 202-239-3431.

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If you have any questions or would like additional information, please contact your Alston & Bird attorney or any of the following:

Thomas E. Crocker
202.239.3318
thomas.crocker@alston.com

BJ Shannon
202.239.3344
bj.shannon@alston.com

Kenneth G. Weigel
202.239.3431
ken.weigel@alston.com

Jon M. Fee
202.239.3387
jon.fee@alston.com

Eric A. Shimp
202.239.3409
eric.shimp@alston.com

Chunlian Yang
202.239.3490
lian.yang@alston.com

Elizabeth M. Hein
202.239.3478
elizabeth.hein@alston.com

Chad A. Thompson
202.239.3927
chad.thompson@alston.com

Diego Marquez
202.239.3003
diego.marquez@alston.com

Jason M. Waite
202.239.3455
jason.waite@alston.com

ALSTON & BIRD LLP

WWW.ALSTON.COM

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ATLANTA: One Atlantic Center ■ 1201 West Peachtree Street ■ Atlanta, Georgia, USA, 30309-3424 ■ 404.881.7000 ■ Fax: 404.881.7777
BRUSSELS: Level 20 Bastion Tower ■ Place du Champ de Mars ■ B-1050 Brussels, BE ■ +32 2 550 3700 ■ Fax: +32 2 550 3719
CHARLOTTE: Bank of America Plaza ■ 101 South Tryon Street ■ Suite 4000 ■ Charlotte, North Carolina, USA, 28280-4000 ■ 704.444.1000 ■ Fax: 704.444.1111
DALLAS: 2828 North Harwood Street ■ 18th Floor ■ Dallas, Texas, USA, 75201 ■ 214.922.3400 ■ Fax: 214.922.3899
LOS ANGELES: 333 South Hope Street ■ 16th Floor ■ Los Angeles, California, USA, 90071-3004 ■ 213.576.1000 ■ Fax: 213-576-1100
NEW YORK: 90 Park Avenue ■ 12th Floor ■ New York, New York, USA, 10016-1387 ■ 212.210.9400 ■ Fax: 212.210.9444
RESEARCH TRIANGLE: 4721 Emperor Blvd. ■ Suite 400 ■ Durham, North Carolina, USA, 27703-85802 ■ 919.862.2200 ■ Fax: 919.862.2260
SILICON VALLEY: 275 Middlefield Road ■ Suite 150 ■ Menlo Park, California, USA, 94025-4004 ■ 650-838-2000 ■ Fax: 650.838.2001
WASHINGTON, DC: The Atlantic Building ■ 950 F Street, NW ■ Washington, DC, USA, 20004-1404 ■ 202.756.3300 ■ Fax: 202.756.3333