Secondary Sanctions: A Weapon Out of Control? Part I: Permissibility of the sanctions under the law of jurisdiction

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Lately, the US has increasingly been 'weaponizing' economic sanctions to push through a foreign policy agenda. Making use of the centrality of the US in the global economy, it has forced foreign states and their firms to choose between halting trade with US sanctions targets or forfeiting access to the lucrative US market. In addition, the US has not shied away from slapping huge fines on foreign firms present in the US that route payments to sanctions targets through the US financial system. While US reliance on economic sanctions as a foreign policy tool is hardly novel, the US has recently made much more aggressive use of them to project US power abroad. Most eye-catching have been the reinstatement of US sanctions against Iran in 2018, the strengthening of the Cuba boycott, and the sanctions on persons involved in the construction of the Nord Stream 2 gas pipeline, which will transport natural gas from Russia to the European Union.

US sanctions do not only govern economic relations between the US and the target state ('primary sanctions'), but also relations between *third states* and target states ('secondary sanctions'). These secondary sanctions do not just aim to coerce targeted states to change political course, but also third states. As secondary sanctions limit third states' sovereignty to freely conduct their external economic relations with other states, they raise deep legitimacy questions. Third states may consider secondary sanctions to violate the principle of non-intervention, and to be extraterritorial in nature, in violation of constraints imposed by the international law of jurisdiction, in addition to other potential breaches.

In a series of three blogposts we address three issues that are central to the legal debate on secondary sanctions: (1) the permissibility of secondary sanctions in light of the customary international law of state jurisdiction; (2) their permissibility in light of multilateral and bilateral conventions concluded by the targeting and third states; (3) the availability of judicial mechanisms to contest the legality of secondary sanctions (for a more in-depth treatment of these and other issues, see the authors' recent article in the *British Yearbook of International Law*).

This first blogpost ascertains what types of secondary sanctions engage, and possibly violate, the customary international law of jurisdiction, and which do not. It is argued that sanctions which limit foreign persons' access to the targeting state's economic or financial system fall within that state's territorial sovereignty, and in principle do not

raise concerns under the law of jurisdiction. However, sanctions which are more far-reaching, such as fines, are more problematic, as a substantial connection (nexus) between the sanctioned activity and the targeting state may often be lacking. The analysis in this blogpost is based on the concept of (state) *jurisdiction* under customary international law. The next blogpost will address the extent to which secondary sanctions engage, and possibly violate, more specific obligations under international law, such as laid down in WTO agreements. We will not separately inquire to what extent secondary sanctions breach the principle of non-intervention, because it is notoriously difficult to define when an intervention unlawfully impinges on a foreign state's sovereignty (for an attempt: see Jamnejad and Wood). Moreover, the principles of jurisdiction already constitute a specific manifestation of the principle of non-intervention.

Secondary sanctions as access restrictions

A considerable number of US secondary sanctions are *access restrictions*. Take, for instance, the best-known country-specific sanctions programme of the US: the Iran sanctions. Under the Iran Sanctions Act, the US Secretary of State or Secretary of the Treasury can impose on non-US persons 'menu-based' sanctions, which consist of various restrictions of access to US markets (taking the form of denials, prohibitions and exclusions). Jurisdictionally speaking, access restrictions create obligations for US persons, and regulate activities that occur in the US and involve US persons as counterparties. They could be justified under a combined application of the territoriality and nationality principles, even if their ultimate addressees are non-US persons (see Meyer). More fundamentally, from the perspective of non-US persons, most of these measures—denial of access to the US financial system, access to US markets, or access to the US for individual persons—merely amount to the denial of privileges (see also Rathbone *et al*). As international law does not entitle foreign persons to financial, economic, or physical access to the US, such measures do not, in principle, raise jurisdictional problems. Measures regulating access to a state's territory, including access to economic facilities based in the territory, are grounded on the principle that states, in the exercise of their territorial sovereignty, have considerable discretionary power to control their borders (see also Lowe and Hafner). It is immaterial in this respect that, ultimately, such access denials relate to the corporation's extraterritorial activities. What matters is simply that the targeting state merely takes away a person or corporation's *privilege* of entering the state's territory and using or offering services there.

This is not to deny the far-reaching impact of secondary sanctions consisting of access restrictions. Notably, the prohibition of 'U-turn transactions' regarding Iran, enacted by the US Treasury in 2008, has had a major impact on non-US banks. U-turn transactions are 'transfers designed to dollarize transactions through the U.S. financial system for the direct or indirect benefit' of sanctioned persons, e.g. Iranian banks or other persons in Iran, or the Government of Iran. U-turn transactions regarding Cuba were initially allowed, but have now also been prohibited. As international energy

contracts are typically issued in dollars, foreign banks financing such contracts normally have to rely on a US correspondent account to pay for goods in US dollars, thereby accessing the US financial system. The ban on accessing the US financial system cripples foreign trade with sanctioned countries, and has been instrumental in European firms winding down business with countries like Iran. For many corporations, such secondary sanctions may be more effective than monetary penalties, especially if their activities are strongly connected to US markets, which may explain why the US has increasingly relied on them. But such impacts do not make access restrictions illegal under the customary international law of jurisdiction.

Secondary sanctions as penalties

US secondary sanctions are not limited to the mere denial of privileges of territorial access, however. Depending on the sanctions programme, US authorities can impose draconian civil and criminal penalties on non-US firms, including non-US controlled firms, for violating US sanctions legislation. The threat of penalties has forced such firms to accept large settlements. In 2014, in what was the largest ever settlement regarding secondary sanctions violations, French bank BNP Paribas settled its potential liability for apparent violations of US sanctions regulations with US federal and state government agencies for a combined US$8.9 billion.

These penalties do not deny to the sanctioned persons privileges previously granted by the US. They are more onerous and intrusive enforcement measures that go beyond a denial of access and may result in a forfeiture of assets and even imprisonment. They do not fall within the above-discussed territorial sovereignty of the US to simply control 'access' to its territory. In practice, US secondary sanctions that are based on penalties rather than access denials are grounded on four jurisdictional triggers: control by a US company, use of US technology, use of the US financial system, and trafficking in confiscated US property. The question arises whether these triggers are compatible with the customary international law of jurisdiction, as the relevant conduct that is subject to US sanctions appears to be extraterritorial: the regulated economic transactions take place between non-US persons and occur outside the US. For an assertion of prescriptive jurisdiction to be lawful under the customary international law of jurisdiction, a substantial connection is required. Our argument is that the US connections on which the four jurisdictional triggers are based are too tenuous to justify US secondary sanctions from a jurisdictional perspective.

First, it is long-standing US sanctions practice to construe the term 'US person' widely as encompassing US-owned or controlled foreign entities. This implies that primary US sanctions do not just apply to entities incorporated in the US, but also to entities incorporated under the laws of a foreign country, provided that they are majority-owned or controlled by a US person. This practice appears to be an improper application of the nationality principle. In international law the nationality of a corporation is based on its place of incorporation rather than the nationality of its shareholders (see ICJ, *Barcelona Traction*, para. 184).

A second trigger for the application of secondary sanctions going beyond denial of privileges is the re-exportation of US-origin items, typically technology. Such export controls appear to be extraterritorial in nature and thus to violate international law (see, *e.g.*, European Communities, 'Comments on the US Regulations Concerning Trade with the USSR'). Arguably, once exported from the US, US-origin items forfeit their jurisdictionally relevant nexus to the US. Such items have no US nationality and thus cannot be justified under the personality principle.

Third, the US Government may take enforcement action which goes beyond access restriction and impose penalties, including forfeiture of assets, on foreign financial institutions for violations of secondary sanctions legislation. The US Department of the Treasury and other US regulators have repeatedly entered into financial settlements with such institutions on the grounds that they facilitated access to the US financial system for targets of primary sanctions such as Iran. For instance, the aforementioned US settlement with French bank BNP Paribas in 2014 resolved its investigation into the bank's 'systemic practice of concealing, removing, omitting, or obscuring references to information about U.S.-sanctioned parties in 3,897 financial and trade transactions routed to or through banks in the United States' in apparent violation of various US sanctions regulations. According to the US view, the exercise of US jurisdiction in these cases is based on the consideration that foreign financial institutions, when routing US dollar payments to or through the US in apparent violation of US sanctions programmes, use the US financial system in their dealings with other foreign persons and thereby export services from the US. However, the territorial connection in these cases is rather tenuous and appears to be merely incidental to the essentially foreign character of the underlying economic transaction between two or more non-US persons (see also Emmenegger). As contracts in the energy and commodities sector are almost always priced in US dollars, foreign banks have to use the US financial system out of necessity, through US dollar SWIFT payment messages sent to US financial institutions. The mere dollar denomination of international business transactions may render foreign financial institutions supporting such transactions subject to US jurisdiction, and to severe financial penalties. It is doubtful whether merely 'using the US financial system' for an otherwise non-US business transaction is a sufficiently strong connection to pass muster under the international law of jurisdiction.

A fourth mechanism of enforcing secondary sanctions beyond a denial of privileges is through the creation of a private cause of action for a US person in relation to a non-US person 'trafficking' in confiscated property. This mechanism is bound up with the Cuban Liberty and Democratic Solidarity (Libertad) Act of 1996 (Helms–Burton Act), Title III of which creates a private cause of action in US courts for US nationals against any person 'trafficking' in confiscated property. This cause of action relates to wholly foreign transactions – non-US nationals investing in Cuba – and is difficult to justify under existing principles of jurisdiction. The personal link to the US, namely that the property confiscated by the Cuban Government originally belonged to US persons or Cuban nationals who later acquired US citizenship, is probably too remote to ground passive personality-based jurisdiction (see also Bismuth).

Obviously, the US may tend to justify the enforcement of its secondary sanctions legislation under the protective or security principle. Indeed, a considerable number of US sanctions regulations are premised on the target posing a threat to US national security, such as the Iran sanctions regime. While attractive in theory, in practice, justifying economic sanctions under the protective principle is unlikely to be convincing, however. In particular, the claim that countries such as Iran or Cuba pose genuine security threats to the US can be doubted. Even if such countries can be considered to jeopardise the essential security interests of the US, it is doubtful whether the imposed sanctions are necessary to protect these interests, or satisfy the proportionality requirement. As explained in our next blog post, the case-law on the reviewability of so-called security exceptions can provide guidance in this respect.

Concluding observations

In this blogpost, we have argued that, for the purposes of assessing the permissibility of secondary sanctions under the customary law of jurisdiction, a distinction should be made between restrictions of access to US markets, and civil and criminal penalties imposed on third country persons engaging in sanctionable activities. The former fall within the sovereignty of states; in principle, they do not raise concerns under the customary international law of jurisdiction. The latter, in contrast, raise acute questions of legality. The connections relied on by the US to justify their assertions of jurisdiction are, in many cases, too tenuous. As a result, such assertions can be considered to fall afoul of the law of jurisdiction. In our third blogpost, we discuss the legal mechanisms where they can be challenged. In our next blogpost, we review US secondary sanctions in light of international conventional law, in particular international trade law (WTO) and international monetary law (IMF).