



Assessing the Countering Russian Aggression Act of 2017

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On January 10, 2017, Senators Cardin, McCain, Graham, and Menendez (along with six of their colleagues) introduced new legislation that would impose statutory sanctions against Russia with respect to its cyber activities, particularly during the 2016 U.S. elections, involvement in the internal Ukraine crisis, and role in the Syria conflict. This legislation, if it were to become law and be implemented vigorously, would do tremendous damage to the Russian economy. Depending on how Russia would react, it could also create significant ripples in the global economy, political stability and energy markets in particular.

This commentary is intended to assess and analyze the potential impact of the legislation as well as Russian and broader market responses, on the likelihood it passes through the U.S. Congress and becomes law. It does not offer a view as to whether this legislation is desirable or warranted.

What's in the legislation

The bill (also known as S.94) is relatively succinct and direct in its explication of both the grounds on which sanctions could be imposed and the kinds of sanctions penalties that would befall violators.

They can be grouped in two large baskets:

1. First, S. 94 codifies existing Executive Orders issued by President Obama with respect to Russia's intervention in the U.S. political process in 2016 and in Ukraine starting in 2013. For all practical purposes, this means that the Trump Administration would be unable to terminate those Executive Orders without seeking Congressional authorization. The legislation offers specific termination language for these measures, as well as the broader set of legislation, but tied to definitive reporting on nonintervention by Russia in democratic processes in general, as well as Ukraine and Syria specifically.
2. Second, S. 94 provides for sanctions covering entities and individuals involved in:
 - a. Development and production of petroleum and natural gas in Russia;
 - b. Development of pipelines in Russia;
 - c. Development of civil nuclear projects by Russia (notably, anywhere around the world);
 - d. Purchase, subscription to, or facilitation of the issuance of sovereign debt of Russia;
 - e. Investment in or facilitation of privatization of state-owned assets by Russia; and,
 - f. Transactions associated in specific ways with serious human rights abuses in "any territory forcibly occupied or otherwise controlled by" Russia.



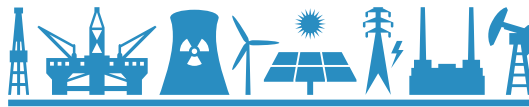
The sanctions permitted under 2.a, b, c, and e are linked to specific thresholds of a fair market value, and sanctions with respect to Russian sovereign debt are absolute: there are no thresholds or triggers, meaning that even \$1 in debt would, in theory, be sufficient ground to impose sanctions.

Except for those measures which are a codification of existing Obama era Executive Orders (which are covered by their original text with respect to penalties), the consequences to be applied against any individual or entity found to be in violation of these provisions would come from a menu of options. This menu is detailed in Section 213 and includes:

1. Prohibition on export-import bank assistance for exports to sanctioned persons;
2. Prohibition on export licenses for sanctioned persons;
3. Prohibition on loans in excess of \$10 million in 12 months from U.S. financial institutions;
4. Requirement to oppose loans from international financial institutions that would benefit the sanctioned persons;
5. Various prohibitions on financial institutions specifically;
6. Prohibition on U.S. government procurement;
7. Prohibition on foreign exchange;
8. Prohibition on banking transactions;
9. Prohibition on property transactions;
10. Ban on investment in equity or debt of sanctioned persons;
11. Exclusion of corporate officers from the United States; and,
12. Sanctions on principal executive officers of the sanctioned person.

Under the terms of the law, if the President were to determine that sanctionable conduct took place, then he would be required to impose five or more of these penalties against the person in question. These sanctions would, under the terms of the law, remain in place until such time as the President makes the aforementioned determination about the Russian government desisting in its intervention in Ukrainian and Syrian affairs.

However, notwithstanding the stern nature of the requirements of the legislation, the President would retain considerable executive discretion under S.94. First, the President retains the ability to determine that no such sanctionable conduct has taken place. Of course, this can be disputed. Oil and gas transactions are hard to hide for very long and there are a variety of reporting mechanisms, watched closely by think tanks and other nongovernmental groups, that would identify such business. Failure on the part of the President to enforce the law is itself a violation of the law and, in theory, legal challenge or a constitutional crisis could be the result. But, past history suggests that such violations can be explained away and that Congressional responses are usually muted, especially when the same party controls both the Executive and Legislative Branch. From 1997-2010, Presidents Clinton, Bush, and Obama undertook no investigations in oil and gas investment in Iran, notwithstanding the requirements of the Iran-Libya Sanctions Act (ILSA, later just the Iran Sanctions Act, ISA) to do precisely that. This situation did not change until 2010, when the State Department announced it would start conducting these investigations and use new powers from the Comprehensive Iran Sanctions, Accountability and



Divestment Act (CISADA) to convince companies to withdraw. Congress complained, but did little else to address this situation.

Second, the legislation provides national security waivers and reporting requirements that would permit the President to identify sanctionable conduct but not impose sanctions penalties, if he explains why, and in particular, how non-imposition is in the U.S. national security interest. This would be potentially embarrassing to the Administration (especially if certain, publically identifiable companies with former executives now working in the Trump cabinet had their penalties waived), but it is something that is available in the law. In fact, the waiver standard used is fairly accommodating and lenient, certainly in comparison to latter-stage Iran sanctions in 2012-2013.

It is therefore not entirely clear that, even if the legislation were to pass through Congress and be signed into law by the President, specific penalties would ever be enforced. However, as with all international sanctions, part of the intent is to influence behavior without having to impose penalties. It is therefore worth considering the overall, aggregate impact of these measures and what discouraging foreign business with Russia in these various areas would mean.

Likely impact on Russia

If S.94 becomes law and the Trump Administration does not indicate that it will refuse to execute its provisions under all circumstances, this legislation would have a major impact on Russia. Russia would find the carefully drafted provisions of Obama-era sanctions completely displaced by sweeping, extensive prohibitions. Russia would still be permitted to sell oil and gas (albeit without its trading partners subject to U.S. penalties), but that would be the extent of their realistic international oil and gas sector involvement. Russia's foreign partners would have to decide whether their investments and activities in Russia are sufficiently profitable so as to be worth the risk of effective exclusion from the U.S. market. Though this is theoretically possible, it is unlikely to be the decision that most major oil and gas companies (as well as service companies, who would also be targeted) make. The potential inability of these companies to import goods from the United States, bank in the United States, or even for their officials to visit the United States, is simply too great of a risk to tolerate for their overall business—most of the major European oil and gas companies have substantial operations in the United States.

That said, though maintenance may be targeted if it exceeds financial or significance thresholds, existing investments would appear to be grandfathered in by the terms of the law, which establishes only that investment undertaken on or after the date of enactment would be sanctionable. Consequently, existing relationships would appear to be outside of the scope of S.94, though a case could arguably be made that this exemption only would be relevant to funds already applied. There are other definitional elements of the sanctions that could further dampen their impact. For example, only investment that “directly and significantly contributes to the enhancement of the ability of the Russian Federation to develop petroleum or natural gas resources” would count. But, these caveats aside, the overall impact would be severe.



This is especially the case insofar as sovereign debt is concerned. As noted in 2015¹, Russia's debt position has already been targeted by the United States and the European Union. S.94 takes that attack much farther and would, for example, preclude the kind of bond float that Russia used in 2016 to generate needed hard currency. Russia has the ability to trim sails if needed where imports are concerned, but not without consequence for the Russian population.

Likely Russian response

Russia would obviously be furious and would respond, but how the country responds is harder to pin down. Recent years have shown us that the Russian regime is savvy and can play what may look like a weak geopolitical hand, truly well.

In the debates around European and U.S. sanctions in 2014-2015, there was speculation that Russia could clamp down on oil or natural gas exports, as Russia has done in the past when seeking to punish Ukraine and Europe. However, Russia is dependent on these exports as well for invaluable sources of hard currency and export revenue. It is unlikely that Russia's response to this challenge would be to commit economic suicide by curtailing exports altogether.

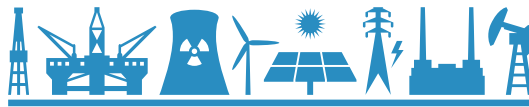
More than likely, Russia would respond asymmetrically. This could involve instigating or prolonging conflict with the United States and its partners elsewhere (such as in the Middle East), cyber-attacks against U.S. actors and infrastructure, and an escalation in military tensions. Ultimately, Russia's response would depend on the degree of enforcement of the sanctions and whether an agreement to deescalate tensions could be reached.

Likely impact on energy markets

The immediate impact of S.94 on markets would probably be marginal, linked to enhanced perceptions of overall risk. The legislation does not affect Russia's existing exports and, though Russia needs additional investment for its future production, the decline in Russian oil and gas fields will take place over a longer time horizon than would prompt an immediate market crisis.

However, this assumes that Russia's response to the imposition of sanctions is calm, mild and largely concerned with avoiding a domestic economic collapse. Were Russia to respond by cutting off or curtailing oil and gas supplies, the market effects could be considerable. Russia is still responsible for roughly 35 percent of Europe's natural gas and 30 percent of Europe's crude oil. Were Russia to retaliate against U.S. sanctions (as well as against European corporate cooperation, even if governments were to object) by cutting off Europe, it would damage its own economic interest, to be sure, but also that of Europe. As two of us have written in Energy Strategy Review, parts of Central and Eastern Europe are still dependent on imports from Russia and do not have sufficient access to alternatives, even though

¹ <http://energypolicy.columbia.edu/publications/report/revisiting-oil-sanctions-russia>



significant progress has been made in recent years. Depending on the scope of the curtailment, the impact could be significant for those countries in Europe that are affected.

Such a cut-off would also adversely affect the market more generally, since Russia is responsible for over 5 million barrels per day (bpd) in crude oil exports according to its official figures. The market is not so well supplied that it could absorb such a loss easily, but – again – much would depend on the specifics of what Russia would do and how Trump would enforce the law.

Likelihood of passage

Though it seems plausible that some new form of Russia sanctions will pass Congress, it is unlikely that those sanctions will look like S.94. Though comparisons are difficult to make, S.94 represents one of the most significant expansions of U.S. sanctions in a decade—both sweeping in scope and targeting a major economic power. Congress has been known to take such broad-brush action in the past, but not without considerable discussion with the Executive Branch and consultation with outside authorities and businesses. This legislation will raise concerns from foreign policy experts and business interests alike, as well as from governments in Europe, Asia, and Russia itself.

Moreover, given Trump’s likely interest to improve relations with Russia and similar views from members of his cabinet, it is likely that S.94 will be sharply criticized by the incoming Trump Administration. A desire on the part of Republican leaders to focus on a prospective, positive “100 Day” agenda will chill enthusiasm for such legislation and could conceivably die in Committee, either in the Senate or the House. Trump himself could veto such legislation and force Democrats and Republicans to come together with sufficient numbers to override his veto, a daunting task demanding two-thirds of both the House of Representatives and the Senate.

But, if further details emerge about the nature of Russian government involvement in the 2016 election or if the situations in Ukraine and Syria worsen, the political winds could change in Congress and make passage of sanctions legislation more likely (and more severe).

Likely global response

At this juncture, it is hard to tell how the international community would react.

Some would doubtless be pleased. European countries afraid of Russian intervention could welcome this sanctions legislation as a means to deter future Russian bad acts. Likewise, Russia’s oil market competitors in the Middle East and beyond could welcome the opportunity to inflict long-term damage on Russia’s economy and oil and gas sectors.

On the other hand, countries either dependent on Russia for their own energy security or fearful of what the Russian government could, or would, do in the event of a major sanctions push from the United States, could react negatively. Taken in combination with frustration over the nature of U.S. “secondary” sanctions (dubbed by most of the world as “extraterritorial”), S.94 or its successor could



lead to a more general rejection of U.S. sanctions policy and push-back on the overbearing nature of the U.S. Congress.

To a great extent, much will depend on perceptions of Trump and of Russia in 2017. If one or the other is perceived as a greater or lesser force for stability and cooperation internationally, then they may have the upper hand in a future conflict. Russia will be watched carefully as Europe moves to the polls in 2017, and a less aggressive posture toward key governments (such as Germany) could reduce the incentive to respond negatively to Russian behavior. On the other hand, a more intrusive approach to those elections – and a more accommodating posture from the United States – could go a long way in putting Vladimir Putin into a defensive posture. It is really too soon to tell.