

EU AND US SANCTIONS: WHICH SOVEREIGNTY?



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If one accepts Jean-Claude Juncker's last State of the Union speech in September 2018, "*the time for European sovereignty has come.*"

As if to prove his case, Donald Trump affirmed this before the UN General Assembly a couple of weeks later by declaring that "*responsible nations must defend against threats to sovereignty.*"

And yet, after a decision by the American president to withdraw from the nuclear agreement with Iran, also known as the Joint Comprehensive Plan of Action (JCPOA), the Europeans will be hit by new extraterritorial US sanctions on 4 November. A similar case arises with Russia, as soon as new US sanctions go beyond those jointly agreed with the European Union.

What a shallow sovereignty!

Extraterritoriality generally refers to the unilateral use of measures that are taken under a state's sovereign powers to enforce its own law, in a territory other than its own, for actions committed outside its territory by entities or people from other countries. This is the case when the United States applies standards and sanctions that it decided on its own.

Any company or individual that is convicted can be punished through their links to the jurisdiction of the United States, such as dollar transactions or the existence of a subsidiary on American territory.

Under such conditions, should the European Union, in the name of its own sovereignty, call into question the practice that the United States has taken it upon itself to make decisions for the rest of the world? If yes, how? If no, what should be done?

1 . THE SITUATION IN THE UNITED STATES

- Extraterritoriality as practiced by the US is an efficient and coherent system. Once legislative and/or regulatory decisions are made, all government authorities work together in perfect harmony, from the legislative branch to the civil and criminal courts, through to the Treasury, the State Department, other federal agencies, and intelligence services. It is a sophisticated and exceptional form of legal diplomacy that is unparalleled in the world.
- The United States uses two types of extraterritorial measures:
 - those resulting from application of the Foreign Corrupt Practices Act of 1977. Examples include Siemens in 2008, and more recently the French pharmaceutical company Sanofi, suspected of corruption in connection with the activities of subsidiaries in Kazakhstan and sanctioned by the US Securities and Exchange Commission;
 - those linked to an embargo unilaterally decided by the United States, such as the sanctions imposed on the banks BNP-Paribas in 2014 and Deutsche Bank in 2015.
- US extraterritorial measures have three main legal foundations:
 - the fight against corruption, both for ethical reasons and to put companies on a level playing field;
 - compliance with various US regulations, including tax evasion, export regulations, competition policy, money laundering, and accounting rules;
 - “national security”, which is open to interpretation. While the EU and the United States shared the same approach in the past, the Iranian case has exposed a major difference.

The logic behind the American measures is based on the following reasoning: on the one hand, as American companies have to follow the rules decided by the United States, a similar standard must be applied to their foreign competitors, lest they gain an unfair competitive advantage; on the other hand, the continuation of trade with a sanctioned country is contrary to the interests of the United States and can threaten national security.

2 . THE SITUATION IN THE EUROPEAN UNION

To date, the European Union does not practice its own extraterritoriality, or at least an extraterritoriality equivalent to the United States, although this point is a matter of debate among experts.

When the EU sanctions foreign individuals or entities, it is as a consequence of actions committed on European territory, actions which have a direct effect on the European Union, or actions which concern EU nationals. In 2001, for example, the EU refused the merger between General Electric and Honeywell, despite the approval of US antitrust authorities, on the grounds that the merger would have affected competition in the EU. Similarly, the tax transparency system, which draws up blacklists of non-cooperative third-party states and is sometimes considered close to extraterritoriality, is primarily aimed at the tax compliance of European citizens.

Indeed, the European Union only intervenes beyond its territorial borders when there is a connection to its territory or its population. For example, European rules on data privacy (the “right to be forgotten”) prohibit the storage and processing of EU citizens’ personal data outside of the Union. Thus, the European Court of Justice ruled that the European Commission had to renegotiate an agreement with the United States that allowed for data storage and processing, in order to ensure that it applies levels of protection as high as those in the EU.

Currently, Europe’s only response to US extraterritoriality is EU Regulation 2271/96 of 1996, the so-called Blocking Regulation. This instrument was decided in response to two US laws, the Helms-Burton and D’Amato-Kennedy acts, which imposed embargoes against Cuba, Libya and Iran at the time. The EU Blocking Regulation was amended on June 6, 2018 in response to the US withdrawal from the JCPOA.

In addition to mandatory reporting requirements to the European Commission and the option for the Commission to authorize European companies to comply with the embargo, the Blocking Regulation has two implications for European firms: a prohibition and a protection.

- The EU prohibits European companies to comply with US extraterritorial sanctions, but this regulation has never been applied in practice. Companies are faced with the choice to lose access to the American market or even an American penalty on the one hand, and the threat of a European fine on the other. As no European company that is complying with American embargoes has been sanctioned to date, the choice for companies is straightforward.
- While the protection instrument could potentially be interesting, it is currently impractical. A European company that withdraws from a contract, for example in Iran, could bring a claim for compensation before a national court, arguing that the withdrawal is due to the threat of American sanctions. It is up to the judge to assess the damage and compensation. For compensation it could go so far as seizing assets of the US government in Europe, although no proceedings of this type have been initiated to date.

In light of this situation, it seems difficult for the European Union to refrain from reacting, especially on the eve of elections to the European Parliament, for which the campaign slogan “a Europe that protects” appears to have great appeal from various sides of the political spectrum.

A European reaction could take different forms depending on whether or not one decides to set up a genuine EU extraterritoriality.

3. AN EU EXTRATERRITORIALITY

The EU could cross the Rubicon of applying extraterritoriality. So far it has refrained from doing so out of a respect for state sovereignty, a founding principle of the current Westphalian international legal order. It would need to make an exception to its multilateral “doxa” in order to rebalance international power with the United States and to have greater influence over US behaviour that undermines state sovereignty.

The European Union could build an autonomous extraterritorial system, analogous to the American system: same legal instruments, same organisational structures and same judicial control.

But this extraterritoriality would be applicable only to specific and predictable instances, defined by directives and regulations that leave little or no room for interpretation. These could be new regulations, involving changes to the EU treaties, or additions to existing regulations. The extraterritoriality of European norms would lead to the extraterritoriality of European sanctions.

There are several domains where this could be applied:

1. **Respect for the environment, biodiversity and the fight against global warming**, i.e. the protection of global goods that do not stop at national borders. The application of norms beyond the territory of the European Union could be justified in cases where the preservation of the planet requires higher standards than those that exist today.
2. **The fight against corruption**, in particular the elevation of this issue to the European level. The EU could adopt new regulations to improve existing standards and provide them with extraterritorial jurisdiction.
3. **The fight against tax evasion**, such the application of extraterritoriality to the French proposal of March 2018, which is currently limited to European territory. A new regulation could require international companies, including the Big Four, to be taxed where turnover is generated and not where they are established.
4. **The protection of personal data**, which could be applied more or less strictly:
 - At a lower level of stringency, protections could cover the personal data of EU nationals worldwide, without having to go through the provisions of bilateral treaties. In the absence of European extraterritoriality, only bilateral agreements can establish such protections. For example, the recently concluded reciprocal adequacy agreement with Japan protects European data on Japanese territory.
 - At a higher level of stringency, the EU would protect the personal data of everyone, everywhere in the world, which would be tantamount to creating a standard of personal data protection at the global level.

To ensure the implementation of such extraterritoriality, Europe would have to acquire the means to do so:

- the US Office of Foreign Assets Control (OFAC) issues licenses and authorizations to invest/export based on US foreign policy and national security requirements. Thus, in 2017, Boeing was authorized to sell a small number of aircraft in Iran. OFAC responds very quickly to companies. It also successfully tracks all offences, both American and non-American;
- the EU should therefore set up a **European Office of Foreign Assets Control**, which would do the same and could be inspired by the British Office of Financial Sanctions Implementation. The budget of the American OFAC is around \$50 million, but it relies heavily on employees from the US Treasury. The corresponding Bureau of the European Union ("Foreign Policy Instrument") is composed of a few officers, who coordinate the policies of the Member States and meet once per month;
- if necessary, the EU would continue to have its own list of prohibited individuals, equivalent to the US SDN (Specially Designated National and Blocked Persons List);
- the EU could extend the powers of the European Anti-Fraud Office (OLAF) in the fight against corruption.

There would still be a fundamental difference between American extraterritoriality and European norms: for Americans, the definition of national security is subject to change, subjective and reversible. It allows the US to change course at any time. European norms, collective and based on objective as well as permanent criteria, are not as malleable. The European Union would remain within a stable legal framework.

Changes of this magnitude would undoubtedly trigger debates in the European Council and the European Parliament. If agreement between the twenty-seven Member States is impossible, or if the current provisions of the EU treaties preclude it, enhanced cooperation between some Member States could be possible, although it would be weaker than a unanimous European response. As for extraterritorial measures of a single Member State, they would obviously not provide for the necessary leverage.

4. STRENGTHENING EXISTING MECHANISMS

If the absence of consensus between EU Member States precludes extraterritoriality, there remains the possibility, even the need, to strengthen current mechanisms in order to enable a sufficiently strong reaction to the American measures and protect European interests, in particular by obtaining exemptions. This was the case in 1996 when the EU filed a WTO complaint against the United States before withdrawing it for consideration. But the American political situation then was different: the president had hesitated to veto Congressional initiatives and had a large executive margin. Today, the White House is on the offensive.

As a matter of principle, the EU would remain in conformity with international law in this case: its countermeasures would be based on reciprocity, which allows retaliation against states that violate their obligations, in particular from agreements that were endorsed by the United Nations Security Council, as was the case with JCPOA.

Several existing mechanisms could be strengthened:

- 1. Subject the activity of foreign banks in the EU to new approval** on the basis of Directive 2013/36/EC of 26 June 2013, which stipulates that financial institutions must have authorisation to carry out their activities in the EU. As a measure of reciprocity, approval could be refused to companies from a third country that imposes extraterritorial provisions on EU companies. This is a symmetrical response, since European banks and companies using US dollars are subject to US extraterritorial standards.
- 2. Establish a European Special Purpose Vehicle (SPV), as suggested on both sides of the Rhine.** Failing to convince the EIB to play a financing role for business with Iran, voluntary contributions from EU Member States could provide the necessary resources to finance, pool or guarantee exports, imports or investments of their companies that so wish, and free them from US sanctions. Such a scheme was announced in New York by Commission Vice-President Federica Mogherini in the presence of the Iranian Foreign Minister. However, Mogherini clarified that several modalities need to be developed further. They may include third-country participation in the SVP or a gradual implementation of the instrument that would begin with basic necessities, such as food or pharmaceutical products.
- 3. Implement the proposal of German Foreign Minister Heiko Maas for EU financial regulations on euro transactions** to avoid blockages in the SWIFT system.
- 4. In the field of financial services,** it should be ensured that the second payment services directive (PSD 2, Directive EU 2015/2366), which governs payments without credit cards (*Fintech*, including Paypal), applies to all payments connected with the European Union's jurisdiction, regardless of a company's nationality.

5. **In the field of competition law** and to the extent that the EU applies a stricter policy than other countries, notably the United States, the EU could impose the same requirements on foreign companies with a link to its territory as it does on European companies.
6. **Clarify and standardise the rules governing the implementation of sanctions that are decided by the EU.** For example, the question of the retroactivity of sanctions, i.e. the consequences for existing contracts, is not yet settled. European companies do not know which rules apply because there is no European body with sufficient authority to lay down uniform criteria that can inform companies.
7. **Emphasise the jurisdiction of national courts** to refuse the applicability of an extra-territorial norm or sanction.
8. **Refile a complaint at the WTO** against the US for failure to comply with its trade opening obligations with the European Union under the WTO agreements, as was the case in 1996. But, here again, the situation today is not the same as it was at the time. It is favourable for the EU that other ongoing litigations under the dispute settlement mechanism have to address national security exceptions, and the issue is therefore no longer taboo. However, it seems that the United States under Donald Trump wishes to reverse the binding nature of adjudications that the US had accepted in 1994 when the GATT became the WTO, as can be seen in the US recent refusal to appoint new judges to the Appellate Body.

With the Iranian nuclear issue, transatlantic divisions are greater than they have been since the Suez Crisis in 1956 when France and the United Kingdom had to bow to American pressure. Whatever the European response will be today, the balance of power between the US and a European Union weakened by Brexit will have to be assessed in the light of two constitutive elements of the international system, the first geoeconomic and the second geopolitical:

- The first is about the **superiority of the dollar** in the international economy, both as a reserve currency and as an invoicing currency, and that the creation of the euro has in no way called this into question. This is the main lever for the effectiveness of US extra-territorial sanctions, which (as noted) are administered by the Treasury Department in Washington. The European Union has, in fact, not reacted to this situation with its passive attitude towards the internationalisation of the euro. It is difficult to see how a rebalancing of sovereignty would be possible without calling this passivity into question. Perhaps it is time to open the debate on this issue.
- The second concerns the future of the **American-Chinese rivalry**, which has taken a new turn under the Trump administration, as it shifts the US approach towards China from “containment” to “push back”. Indeed, it cannot be ruled out that the United States will impose future sanctions on China that go beyond the current trade measures initiated by the American president, which could then be applied extraterritorially on the basis of precedents like Iran. There is no doubt that the European reaction in such a case should be of a completely different nature. Perhaps it would be wise to take decisions for the Iranian case by considering this wider economic and political context.

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