How do sanctions impact on trade in the Black Sea Region?

Black Sea Region (Ukraine, Turkey, Bulgaria, Romania, Russia, Georgia) plays a crucial role for Europe: main routes connecting from west to east and from north to south cross it. All the post-Soviet protracted (frozen) conflicts occurred mainly in the Black Sea Region. They gave rise to so-called *gray areas* facilitating organized crime, illegal trade and radicalization. It is not difficult to see how Russia uses them for political intimidation of the new independent states – former Soviet republics.\

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From the very beginning of the Russian military aggression at the Crimean Peninsula, position of the international community has become quite clear in condemning Russia's interference with the internal affairs of Ukraine and violation of its territorial integrity and sovereignty. The Russian Federation was demanded to comply with international law regulations, international obligations, inter alia, in the framework of the Budapest Memorandum. The Russian government, disapproving of legitimacy of Ukrainian Revolution, in particular, toppling of President Yanukovich, the constitutional reform and creation of a new government, rejected demands of the global community and even inspired and inflated the military conflict in Eastern Ukraine.

Crimea impact

No doubt, annexation of the Crimea effected trade in the Black Sea Region countries. Today, the share of Russia, Ukraine, Kazakhstan and the Danube Region countries is up to 40% of the global wheat trade. The Black Sea Region runners up (after the Persian Gulf Region) among oil and natural gas sources. It is also replete with proven reserves of minerals, metals and other natural resources. The Black Sea is an inland sea, with ports located in many coastal cities, such as Constanta, Odessa, Sevastopol, Kerch, Novorossiysk, Sochi, Sukhumi, Batumi, Trabzon, Samsun, Burgas and Varna.

A significant impact on the container turnover in the countries of the Black Sea region was exerted by the military conflict in the east of Ukraine and the trade embargo against Russia. As a result, the total throughput of containers in 2015 did not exceed 2.3M TEU, and all this against the background of low freight and charter rates, due to which the majority of container lines operate at best at breakeven. But by the end of 2016, almost all countries of the Black Sea region increased the traffic of loaded containers. According to the Ukrainian Sea Ports Authority , its ports showed growth, which allowed them to restore the positions lost in 2015.

In 2016, one notable event was a forced change of the usual export routes due to the transit embargo imposed by Russia. Early in the year, it complicated significantly routes of Ukrainian trucks and railcars carrying goods to Kazakhstan, Central Asia and other states through its territory, while in summer it banned transit carriage of goods from Ukraine to Kazakhstan and Kirgizia by road and by rail.

Cabotage carriages

It is noteworthy that cabotage carriages between the Ukrainian sea ports have become very popular for the recent years. According to statistic data, mutual trade between the Russian Black Sea Region and other Black Sea Region countries is insignificant on the general background. The turnover between Krasnodar Region and its neighbours in the Black Sea Region – Abkhazia, Bulgaria, Georgia, Romania and Ukraine – in 2016-2017 amounted to only $495 and $576M respectively. The Russian Federation purchased fruit and vegetables in Egypt only in 2017 nearly at the same cost (ca. $0.5Bn), while the Black Sea Region share in the aggregate turnover in Kuban for these years decreased from 5.3% to 4.9%. Growth in throughput between regional exporters and non-CIS countries occurred in the Mediterranean countries, first of all in the Middle East. According to the State Statistics Service of Ukraine, in 2017 its turnover upon trade with Russia increased substantially: Moscow regained the status of one of the largest trade and economic partners of Kiev, with increase of the goods supply by 39.9%, as compared to 2016.

Russia is not shown in the *Black Sea Transboundary Cooperation* program with principal financial flows from the EU to the Black Sea Region states. This program applies to Armenia, Bulgaria, Greece, Georgia, Moldova, Romania and Ukraine only. Even heavyweights, such as the USA, China and Japan, do not try to use the Black

Sea in their own interests. Their interventions are very far from the Black Sea regional integration in the form Russia would like to see it.

Sanctions affect

It is quite obvious that sanctions affect international policy and economy. However, such effect is ambiguous. Sometimes international economic sanctions cause more damage to their instigators than to their goals. Close integration of territorial markets in the modern globalized world provides not only an instrument of negative influence by means of breaking economic relations, but also creates many opportunities to counteract such effects by means of fixing new relations. Therefore the issue concerning effectiveness of international economic sanctions is too vital. International economic sanctions are related to such problems as the humanitarian damage suffered by innocent people, as well as the third countries damage caused by introduction of sanctions (special economic problems arising from taking preventive or coercive measures). The UN have done all the best to solve such problems. Its efforts resulted in creating the concept of targeted and smart sanctions, the essence whereof is the most focused impact directly on the object (i.e. political groups or specific persons who bear direct responsibility for the committed offenses), the extremely clear goals for introduction of sanctions, their validity terms and criteria for cancellation of the sanctions regime. The effectiveness of arms embargoes and freezing financial assets is especially high.

Since 1997-1998, reformation of sanction policy is in process. It includes several interrelated processes: the Interlaken Process initiated by the Swiss Government, the Bonn-Berlin Process initiated by Germany, and the Stockholm process initiated by Sweden. These countries have funded a research conducted by the Watson Institute for International Studies who carefully studied such a subtle legal problem and put forward interesting proposals in 2006.

Effectiveness of international economic sanctions has been assessed within two aspects: analysis of the effects for economy and security of countries and analysis of the efficiency of imposing sanctions as a foreign policy instrument.

Analysts came to the following general conclusion: sanctions are much more effective when they are imposed against friendly or neutral countries: nearly 50% of success for friendly countries, 33% for neutral ones and only 19% for hostile ones. But sanctions against hostile countries did not ever result in termination of hostilities.

Of course, restrictions on technology transfer in future will have negative impact on the Russian economy. In the nearest 5-7 years, restriction in exploration and production technologies (with regards to the fact that there are neither such technologies nor a base for their creation in Russia) will have negative impact on oil and gas production level and its cost. But today the effect of such a restriction is zero. The same concerns military technologies: today Russia is actively increasing its production of arms and is keeping their export at a high level (over $10Bn per year), without any essential influence of imposed restrictions. However, in future inability to use global achievements in dual technology development will result in the Russian arms falling behind their closest competitors, such as the USA, the EU, Israel and most likely China. Today Russia's position in the international arms market is weakening and probably will lose the Indian market (first of all, military aircraft), while China, still buying Russian air defence systems, has been already focused on its own developments in aviation. Probably in 10–15 years, with focus in this industry shifted to the sixth generation systems in developed countries (and, respectively, to the fifth generation in developing countries), Russia will have nothing to offer on the market.

Counter-sanctions, i.e. self-restraint measures related to food import, implemented first of all against a number of countries (first of all, EU members) and subsequently against Turkey, also have no essential impact on the economy. There was no *import substitution* regarding prohibited items (i.e. the proportional growth in production of their exact equivalents in Russia), at least because devaluation of the Rouble reduced consumption significantly: loss of the prohibited import volume in fact was insignificant. Import substitution commodities got much more expensive than the average daily demand goods (price growth for products from the sanctions list ranged from 30% to 100% for the last 18 months). However, due to falling demand and total reduction in quality of domestic equivalents (switching to surrogate ingredients, refusal to withstand technology, etc., in order to reduce prime cost and to speed up production process), neither food surplus nor food shortage appeared.

Probably, unpredictable and inconsistent hostile behaviour of Russia in respect of foreign economic institutions has the most negative impact on the Russian economy. The attempt to autonomize the country in vital industries (telecommunications, payment systems, transportation systems, IT, navigation, funding non-commercial and charitable organizations etc.) often (but certainly not always) results in lobbying efforts by local players, operating not very skilfully and in the limited scope, and corrupt or short-sighted officials. Such an attempt boosts expenses and results in manufacturing a product which cannot be used to the full extent as a substitute for modern technology; sometimes it even results in painful rejection of well tried and tested international technologies. It threats security of Russia – not due to a fictional external threat, but due to the real threat, namely non-functionality of a substitute product.

It is quite difficult to determine how successful were the measures aimed at changing policy of the countries being targets of sanctions. Such concepts as prestige, status, reputation are intangible and one can hardly find a suitable empirical indicator of their condition. Sanctions are also imposed jointly with attempts of political pressure, threat of force, and it is not easy enough to find out which measures were successful.

International sanctions are the most effective as means of persuasion, not punishment. They need to contain elements of motivation encouraging observance thereof. The target of sanctions should understand which actions it is appealed to perform. Meantime full or partial compliance with requirements should cause an appropriate response from the UN Security Council, respectively, in the form of sanctions relief or cancellation. Today the most important task is aimed to ensure legitimacy of international sanctions. Maintenance of peace and security largely depends on common understanding of legitimacy of imposing international legal sanctions. In this regard, while making a decision on introduction of international sanctions, it is necessary to promote, first of all, maintenance of international peace and security and legitimacy of sanctions as set forth in the UN Charter and other international law regulations.

Black Sea Region case study

Unfortunately, issues related to sanctions are too politicized. The practice of applying UNCLOS, for instance, with regards to the regime of transit passage through straits used for international shipping, is a little bit different from the standards set forth in this Convention. Ukraine, in turn, does enable to provide security, since a vessel's detention does not imply this. Therefore, it happens that national procedures contradict to the conventional postulates of international law.

Interlegal portfolio contains the following notable cases:

- the case on m/v MEKHANIK POGODIN (IMO:9598397). For over 7 years, m/v MEKHANIK POGODIN (IMO:9598397) was owned and used by a legal entity which was not subject to special economic and other restrictions in Ukraine. But according to primary documents submitted under the vessel's call at the sea port, the documentary vessel owner was subject to special economic and other restrictions (sanctions) which resulted in immediate vessel's detention.

Today, the case has been considered by the court of appeal. Both vessel's arrest and detention have similar effects: route restriction, i.e. it has been blocked at the sea port. The vessel has been detained by Harbour Master in compliance with Award by State Border Service of Ukraine. It has been operated under the Lease Agreement concluded in 2011 between OJSC "WEB Leasing" (the Lessor) and LLC "V.F. Tanker" (the Lessee). OJSC "WEB Leasing" has been entered into the Ukrainian list of sanctions. While staying at the sea port, it was the last lease payment term. Following lease payment, title on the vessel was transferred to LLC "V.F. Tanker". Therefore, now there are no lawful and reasonable grounds for further vessel's detention. Unlawfulness of further detention has been certified also by Expert's Opinion of the Koretsky Scientific and Research Institute of State and Law. But Kherson District Administrative Court rejected the claim on vessel's release. Now it got clear how thin the line between legal and political matters is. Further vessel's detention will threat with essential losses to be incurred by the state of Ukraine, due to the vessel further stay idle, while the shipowner will obtain damage reimbursement from the insurers;

- the case on m/v SEABREEZE (IMO: 9143312). The court made an order on arrest of one vessel due to the other vessel’s actions. Although Prosecutor’s Office states that both vessels have the same manager, today it is a false statement, since the company had ceased to manage the vessel long time before the sanctions were imposed. Therefore, information from out-of-date commercial sources has launched state mechanisms and in fact has impeded absolutely lawful and transparent business;

- the case on m/v KANTON (IMO: 9412311). The court arrested m/v KANTON (flag of Tuvalu) for a breach of the regime of calling at the Crimean sea ports. Having called at the closed Crimean sea ports, shipowners, masters and crew members committed the crime stipulated by Article 332-1 of Criminal Code of Ukraine.

- the case on m/v SKY MOON (IMO: 7525334). In 2016 the vessel was detained due to a breach of the procedure of entering/leaving the occupied territory of the Crimea, followed by her seizure in favour of the state of Ukraine in 2017.

With regards to diversity of cases proceeded by Interlegal experts, we understand clearly the algorithm of works upon the sanction-related cases in Ukraine and we may provide any legal support to our clients.

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