

Sanctioning Russia Over Invasion of Ukraine

On February 21, 2022, Russian President Vladimir Putin unilaterally recognized the Luhansk and Donetsk regions in Eastern Ukraine (Covered Regions) as independent states. Thereafter, Mr. Putin authorized a full-scale invasion of Ukraine.

In keeping with its promises in the period leading up to the invasion of Ukraine, the United States, and many of its allies—including the European Union, Switzerland, Japan, Australia, New Zealand, and Taiwan—are imposing waves of significant sanctions on a number of Russian entities. The United States has issued four executive orders (EOs) to date (14038, 14039, 14024, and 14065), which along with a number of directives implement the new sanctions. The United States has also added significant export controls requiring licenses for export to Russia of numerous items across a broad range of technologies. This early wave imposed by the United States is summarized below. More sanctions and export controls are likely to quickly follow as tensions in the region rapidly escalate.

Impact of Recent OFAC Russia Sanctions

Summary

The Office of Foreign Assets Control (OFAC) has imposed full blocking sanctions on a number of Russian banks over the past week. In addition, it placed Sberbank, Russia's largest bank, and numerous subsidiaries on a newly developed Correspondent Account and Payable-Through Account Sanctions (CAPTA) List. It also issued further sectoral sanctions targeting Russian financial institutions, an additional directive (Directive 3) that restricts the issuance of new debt of longer than 14 days maturity to certain designated Russian entities, and sanctions prohibiting most transactions with Russia's Central Bank (Directive 4). Finally, OFAC has broadly sanctioned certain separatist regions of Ukraine.

OFAC Sanctioned Regions

OFAC administers two types of sanctions: (1) sanctions imposed on an entire country or region (including all persons residing in those jurisdictions), and (2) sanctions imposed on companies, entities, or individuals specifically identified in OFAC's Specially Designated Nationals (SDN) list as well as other list-based sanctions (such as OFAC's Sectoral Sanctions Identification List and CAPTA List).

OFAC has not sanctioned the entire country of Russia. It also has not sanctioned the entire country of Ukraine. However, on February 21, OFAC broadly sanctioned the Covered Regions, imposing restrictions similar to the sanctions imposed on the Crimea region of Ukraine in 2014 after it was annexed by Russia. Briefly, a U.S. company or other U.S. person cannot enter into a transaction, or facilitate a transaction, with anyone located in these sanctioned jurisdictions. In addition, non-U.S. persons found to have operated in the Covered Regions may also be sanctioned in certain circumstances.

Sanctioned Government Entities, Companies, and Individuals

OFAC added several Russian and Belarusian entities and individuals to the Specially Designated Nationals and Blocked Persons (SDN) List. If a person or entity is on the SDN List, a U.S. person may not conduct or facilitate any transactions with that person or entity and must block (i.e., freeze) any property in its possession that belongs to an SDN. Further, under the "50 Percent Rule," any other entity in which an SDN owns, directly or indirectly, a 50% or greater interest must be treated as an SDN even if the other entity is not specifically identified on the SDN list.

OFAC placed Mr. Putin himself on the SDN List along with many of his key allies and many business leaders linked to Russian financial institutions. Sanctions targeting Russian entities have primarily been levied on government and state-owned companies and a large number of private Russian financial institutions.

OFAC Actions Involving Russian Banks

SDN List

On February 22, 2022, OFAC placed the following banks on the SDN List:

- The State Corporation Bank for Development and Foreign Economic Affairs Vnesheconombank (VEB), which finances the Russian defense industry and services large defense contracts, and 17 of its subsidiaries;
- Promsvyazbank Public Joint Stock Company (PSB), which provides financing for large-scale projects to develop Russia's infrastructure and industrial production, and 25 of its subsidiaries;
- Bank BELVEB OJSC, a bank located in Belarus;
- Prominvestbank, a bank located in Ukraine; and
- Eximbank of Russia JSC, which is an export support institution located in Russia in addition to functioning as a commercial bank regulated by the Central Bank of the Russian Federation.

On that day, OFAC placed on the SDN list many other VEB and PSB affiliates including numerous financial firms.

On February 24, 2022, OFAC placed the following banks on the SDN list:

- VTB Bank and 20 subsidiaries including approximately 11 banks along with Denis Bortnikov deputy president of VTB Bank and chairman of the VTB Bank board (son of previously designated Putin ally, Aleksandr Bortnikov) and high-ranking VBT executives, Andrey Sergeevich Puchkov (Puchkov) and Yuriy Alekseyevich Soloviev (Soloviev);
- Bank Financial Corporation Otkritie and 12 subsidiaries including one bank;
- Sovcombank and 22 subsidiaries; and
- Novikombank.

A list of the VTB, Otkritie, and Sovcombank subsidiaries may be found at the end of the [OFAC press release](#).

Unofficial press reports suggest that many of these institutions also have been, or soon will be, prohibited from using the Society for Worldwide Interbank Financial Telecommunication (SWIFT) payments system, which is the principal communications method banks worldwide use to effect financial transactions.

OFAC has also sanctioned Alexander Aleksandrovich Vedyakhin (Vedyakhin), first deputy chairman of the executive board of Sberbank, a Russian state-owned financial institution that is subject to the more targeted sanctions described below. And, on February 28, OFAC placed the Russian Direct Investment Fund, and at least two of its affiliates, on the SDN List, along with Chief Executive Officer Kirill Dmitriev.

OFAC Actions Involving Russian Political Figures

In this tranche of sanctions, certain family members of previously designated national Russian oligarchs were also added to the SDN List. They include:

- Petr Fradkov, chairman and CEO of PSB, who is the son of previously designated Mikhail Fradkov.
- Vladimir Kiriyyenko, who is the son of previously designated Sergei Kiriyyenko. Vladimir was previously vice president at the Russian state-controlled company, Rostelecom, and is presently the CEO of VK Group, the parent company of Russia's top social media platform, VKontakte.

CAPTA List

Under Directive 2, OFAC placed Sberbank, Russia's largest financial institution, which was already on OFAC's Sectoral Sanctions Identification (SSI) List, on the CAPTA List, along with approximately 25 Sberbank subsidiaries. If an entity is placed on the CAPTA List, a U.S. financial institution cannot:

- Open or maintain a correspondent account or payable-through account for or on behalf of the foreign financial institution; or
- Process any transaction involving the foreign financial institution.

Prohibiting Sberbank from maintaining correspondent accounts with U.S. financial institutions effectively cuts the bank off from U.S. dollar transactions.

Sovereign Debt Restrictions Extended

OFAC also increased restrictions on dealings in Russia's sovereign debt. Specifically, OFAC issued Russia-related Directive 1A amending and superseding its prior Directive 1. Directive 1A extends existing sovereign debt prohibitions to cover participation in the secondary market for bonds issued after March 1, 2022, by the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, or the Ministry of Finance of the Russian Federation.

Directive 3 Restrictions on Debt and Equity Transactions

The February 24 sanctions include Directive 3 which places restrictions on new debt and equity of 13 listed entities. In short, as of March 26, 2022, U.S. persons are prohibited from participating in any transaction involving either new debt of longer than 14 days maturity or new equity. This includes extension of payment terms longer than 14 days. The targeted entities include Alfa-Bank, Alrosa, Credit Bank of Moscow, Gazprom, Gazprombank, Gazprom Neft, Rushydro, Russian Agricultural Bank, Russian Railways, Rostelecom, Sberbank of Russia, Sovcomflot, and Transneft.

Directive 4 Prohibitions on Transactions Involving the Russia's Central Bank, Ministry of Finance, and National Wealth Fund

On February 28, OFAC issued Directive 4, broadly prohibiting U.S. person involvement in transactions involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, or the Ministry of Finance of the Russian Federation. In General License 8A, however, OFAC authorizes energy-related transactions with the Central Bank of Russia through June 23, 2022.

The Nord Stream 2 Pipeline

OFAC issued blocking sanctions against Nord Stream 2 AG (a Swiss firm whose parent company is the Russian state-owned Gazprom) and its CEO Matthias Warnig. The wind-down provisions are in place until March 2, 2022.

Wind-Down Provisions

Many of the OFAC prohibitions provide a wind-down period for the U.S. company to wind down the transaction in question. These vary from a few weeks to three months. OFAC has traditionally extended these wind-down periods where deemed appropriate. Ukraine General License (GL) 17 authorizes the wind-down of transactions involving the Covered Regions until March 23, 2022. Russia-related GL 11 authorizes the wind-down of transactions involving Otkritie, Sovcombank, and VTB Bank by March 26, 2022. Russia-related GL 3 also authorizes a wind-down of transactions with respect to VEB, as well as VEB's servicing of sovereign debt, which must be completed by March 24, 2022.

Impact of Recent Export Control Restrictions on Russia/Ukraine

In addition to economic sanctions, the United States (and many allied countries) have adopted expansive controls on exports and reexport of certain hardware/equipment, software, and technology to Russia. These restrictions make it significantly more difficult to export these items to Russia by expanding licensing requirements and reducing the scope of available license exceptions. Notably, broad controls will now apply to U.S. exports of any kind that are destined for military end users or military end uses in Russia, which extend to foreign-produced items incorporating or produced using U.S.-origin items.

US Export Control Restrictions

Over the past week, the U.S. Commerce Department's Bureau of Industry and Security (BIS) issued numerous export controls regarding Russia and the Covered Regions of Ukraine:

- Any items subject to the EAR and included on the Commerce Control List (CCL) in Categories 3 (Electronics), 4 (Computers), 5 (Telecommunications and Information Security), 6 (Sensors and Lasers), 7 (Navigation and Avionics), 8 (Marine), or 9 (Aerospace and Propulsion) require licenses for export or reexport to Russia. The expanded licensing requirements do not include EAR99 items, nor any items that are not "subject to the EAR."
- All items "subject to the EAR" now require a BIS license for export or reexport to the Covered Regions, so these regions should be treated similarly to Crimea. These licenses will be subject to a presumption of denial by BIS.

In addition, BIS placed certain Russian entities on the Entity List, which bans exports to those entities without a license from BIS. Such license applications are subject to a presumption of denial by BIS. The targeted entities are primarily Russian military end users, but other Russian entities may be added in the future.

SWIFT

On February 26, 2022, the United States and its allies committed to removing certain Russian banks from SWIFT, the high-security communications network that facilitates payments by transmitting information regarding these transactions among 11,000 financial institutions in 200 countries. Removing banks from the SWIFT system will effectively block the targeted institutions from participating in the international financial system. Notably, the SWIFT network is an information exchange that facilitates the movement of funds between participating financial institutions; it is not responsible for the actual movement of funds between these institutions.

Caveats

- The above summary includes sanctions imposed by OFAC and BIS through February 28, 2022.
- The reaction of the Russian government is still uncertain. Among other countermeasures, Russia could freeze USD bank accounts or counter-ban western products/technology.
- Shipping delays should be anticipated in this region of the world.
- The implications for cyber security issues have yet to be determined in Ukraine.
- It is difficult to predict the reactions that U.S. service companies may have to these restrictions. Some have already suspended all transactions involving Russia. Although such actions are not compelled by the OFAC sanctions to date, many U.S. companies may adopt a conservative position, exiting the Russian market altogether given the breadth of these prohibitions.

Recommendations

Any entity transacting or contemplating transactions with Russian entities or those within the Covered Regions should carefully consider their approach to mitigating risks raised by the new and emerging sanctions and export controls. Given the broad risks raised by these new sanctions and export controls, companies operating in the region should be reevaluating critical sanctions and export compliance controls, including:

1. Whether counterparties are being effectively screened;
2. Whether there are operations or business relationships in any of the sanctioned separatist regions of Ukraine;
3. Whether there are certain services being provided remotely and, if so, whether the risk of sanctioned person or sanctioned region involvement is adequately addressed;
4. Whether any foreign subsidiaries and affiliates have been alerted to the Russia/Ukraine sanctions and informed of compliance obligations with which they may have to comply (e.g., examining and possibly alerting banking relationships); and
5. Whether any U.S.-origin products or technology are being exported to Russia.

Conclusion

The sanctions and export controls aimed at Russia and the Covered Regions in the wake of Russia's invasion of Ukraine are evolving and expanding rapidly. Additional sanctions and other restrictions are imminent.

Companies operating in or with business relationships with Russia and Ukraine should ask themselves the key questions noted above to assess new and emerging risks that these sanctions may raise and ensure that their sanctions and export compliance controls are sufficiently robust to address their risk profile in light of the new restrictions.

Companies should also note the numerous OFAC general licenses authorizing the wind-down of transactions and licenses that permit certain energy-related transactions and noncommercial activities to move forward. While general licenses of this nature are intended to ease the burden on U.S. companies, transacting within the bounds of the authorizations requires very careful analysis. These complex and high-profile new restrictions must be approached with caution because regulators will likely pursue violations aggressively. Companies transacting in this region should seek guidance from international trade counsel with substantial expertise in U.S. economic sanctions and export controls to ensure that they are adequately adapting to the new and expanding Russian sanctions landscape.

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