Diligent

Emerging Developments in U.S. Sanctions Against Russia

The Russian Federation's unprovoked, unilateral decision to occupy Ukraine in February 2022 set the stage for comprehensive sanctions to be imposed by global governments against the Putin regime. While the United States had previously imposed selective sanctions on Russia during the presidency of Barack Obama over the annexation of the Crimean Peninsula in 2014, Russia's full-scale invasion of Ukraine in 2022 caused the Biden Administration to impose crippling economic and trade sanctions on Russia to punish Putin and the Russian Federation's ruling class for violating Ukraine's territorial sovereignty. These sanctions include the expansion of regulations administered by the United States Department of the Treasury's Office of Foreign Asset Control ("OFAC") and the United States Department of Commerce's Bureau of Industry and Security ("BIS").

This white paper is intended to provide legal and compliance professionals with critical insight into the applicability of these regulations. Given the highly volatile nature of current geopolitical developments, however, the reader is cautioned that the white paper itself is not a definitive sanctions guide and care should be taken by legal and compliance professionals to keep pace with emerging developments in the sanctions landscape by resorting to primary legal sources.

I. OFAC and CAATSA Sanctions Overview

a. Background

The primary sanctions apparatus utilized by the United States against the Russian Federation has historically taken the form of Executive Orders issued by the President. These Orders then provide the universe for OFAC to target with restrictive measures, designations, and related guidance. Under a series of Executive Orders issued by former President Barack Obama in 2014, the Russian Federation and its various officials, as well as critical sectors of the Russian Federation economy, became the target of blocking sanctions and more selective prohibitions on certain transactions involving U.S persons.

Executive Order 13660 signed on March 6, 2014 originally authorized sanctions on individuals and entities responsible for violating the sovereignty and territorial integrity of Ukraine and imposed certain restrictions on the travel of individuals deemed complicit in acts that undermined democratic processes or institutions in Ukraine. Executive Order 13661 signed on March 17, 2014 authorized OFAC to block the property and interests of former Ukrainian and current Russian Federation officials who threatened the peace, sovereignty and territorial integrity of Ukraine as well as persons who operated in the arms or related sectors in the Russian Federation. Executive Order 13662 signed on March 20, 2014 significantly expanded the scope of the prior Executive Orders by enhancing OFAC's authority to block the property of persons who operate in certain critical sectors of the Russian Federation economy, including financial services, energy, mining and metals, engineering, defense and related materiel. Finally, Executive Order 13685 signed on December 19, 2014 further limited commercial transactions and blocked the property and interests in property of certain persons associated with the Russian Federation's annexation of the Crimean region. Executive Order 13685 also prohibited new investment in the Crimean region of Ukraine; the exportation, re-exportation, sale or supply of any goods, services or technology to the Crimean region of Ukraine; and the approval, financing, facilitation, or guarantee by a United States person, wherever located, of any transaction by a foreign person when that transaction would be prohibited if performed by a United States person.

In subsequent years, the Russian Federation became the object of additional sanctions as a result of a series of notable transgressions including purported interference in the 2016 U.S. elections and the use of nerve agents and other biological toxins to poison political dissidents. Despite protestations by then-President Donald J. Trump in 2017, Congress overwhelmingly passed the Countering Russian Influence in Europe and Eurasia Act of 2017 (Title II of the Countering America's Adversaries Through Sanctions Act of 2017 ("CAATSA")). Under CAATSA, Congress imposed legislatively mandated sanctions on the Russian Federation for activities concerning: (1) cyber security; (2) crude oil projects; (3) financial institutions; (4) corruption; (5) human rights abuses; (6) evasion of sanctions; (7) transactions with Russian defense or intelligence sectors; (8) export pipelines; (9) privatization of state-owned assets by government officials; and (10) arms transfers to Syria. While CAATSA granted the President discretion to waive certain cyber security and Ukraine-related sanctions, the principal effect of the law was to significantly hamper then-President Trump's ability to rescind sanctions imposed on the Russian Federation by the previous Administration. Significantly, Section 241 of CAATSA also required the Department of the Treasury, in concert with the Director of National Intelligence and the Department of State, to issue a report identifying Russian Federation political figures, oligarchs and parastatal entities within 180 days of enactment.

On January 19, 2018, the Department of the Treasury released its Section 241 report to the Congress. Among other things, the report publicly identified one hundred fourteen (114) political figures and ninety-six (96) oligarchs thought to have close ties to the Putin regime. While the report itself did not impose new sanctions on the individuals identified, many of the persons implicated in the report were subject to pre-existing sanctions as Specially Designated Nationals ("SDNs") identified by OFAC.

On April 15, 2021, President Joseph R. Biden, Jr. issued Executive Order 14024, blocking the property of individuals and institutions connected to "specified harmful foreign activities" of the government of the Russian Federation. On the same day, OFAC implemented Executive Order 14024 by designating five (5) Russian entities operating in the technology sector of the Russian economy that were determined to be abetting the Russian Intelligence Service's malicious cyber activities.

b. Recent Sanctions Activity

In the immediate lead up to, and direct aftermath of, the Russian Federation's full-scale invasion of Ukraine in late February 2022, sanctions activity dramatically increased.

On February 21, 2022, President Biden declared the separatist regions of the **Donetsk People's Republic ("DNR")** and **Luhansk People's Republic ("LNR")** as Russian territory. As a consequence, Biden issued Executive Order 14065, which prohibited: (1) new investment in the DNR and LNR regions by a United States person wherever located; (2) the direct and indirect importation of any goods, services, or technology from the DNR and LNR; (3) the direct and indirect exportation, reexportation, sale or supply of any goods, services, or technology to the DNR and LNR by a United States person wherever located; and (4) any approval, financing, facilitation or guarantee by a United States person wherever located of a transaction by a foreign person where such a transaction would be prohibited if performed by a United States person.[1] OFAC issued nine (9) general licenses coinciding with the promulgation of Executive Order 14065. These general licenses include:

- GL 17 permitting the wind-down of operations and contracts involving the DNR and LNR by March 23, 2022 [**EXPIRED**];
- GL 18 authorizing the export to the DNR and LNR of agricultural commodities, medicine and medical devices related to the ongoing COVID-19 pandemic;
- GL 19 permitting telecommunications and mail services to continue in the DNR and LNR;
- GL 20 authorizing the conduct of official business by certain international organizations, including, but not limited to, the United Nations, The International Committee of the Red Cross, and The Organization for Security and Co-operation in Europe'
- GL 21 respecting the provision of personal remittances to the DNR and LNR;
- GL 22 authorizing the continued exportation of services and software incident to the provision of Internet-based communications;

1. The language in this Order is virtually identical to the Crimea-related restrictions of Executive Order 13685.

- GL 23 authorizing certain transactions of non-governmental organizations in the DNR and LNR (including the support of humanitarian projects; activities to support democracy; activities to support non-commercial development related to health, food security, water and sanitation; and activities to support environmental and natural resource protection);
- GL 24 authorizing transactions related to the provision of civil maritime services; and
- GL 25 permitting the conduct of journalistic activities and transactions ordinarily incident and necessary for such activities.

On February 22, 2022, acting under the authority of Executive Order 14024, OFAC also sanctioned two (2) Russian banks—namely, the **State Corporation Bank for Development and Foreign Economic Affairs Vnesheconombank ("VEB")** and **Promsvyazbank Public Joint Stock Company ("PSB")**, along with forty-two (42) subsidiaries thereof. OFAC added the entities to its SDN List as institutions identified as providing crucial support to Russia's ability to raise funds and to finance its defense operations. OFAC also issued a single general license—GL 3—permitting the wind-down of transactions involving VEB through March 24, 2022. That license has since expired.

On February 23, 2022, OFAC took further steps in response to increasing Russian aggression in the Ukraine. OFAC announced the imposition of sanctions against **Nord Stream 2 AG**, the Swiss-based company in charge of the construction of Russia's Nord Stream 2 gas pipeline as well as its chief executive officer, **Matthias Warnig**, and added both to the SDN List. OFAC further issued General License 4, authorizing the wind-down of transactions involving Nord Stream 2 AG through March 2, 2022. That license, too, has since expired.

On February 24, 2022, OFAC significantly expanded the reach of its sanctions regulations by imposing full blocking sanctions on four (4) additional Russian banks—namely, **VTB Bank**, **Otkritie**, **Novikom**, and **Sovcom**, as well as their subsidiaries. OFAC simultaneously issued Directive 2 pursuant to Executive Order 14024, which imposed correspondent and payable- through account limitations on Sberbank and its subsidiaries and Directive 3, which prohibited dealings in new debt and equity of certain Russian financial institutions and state-owned enterprises. In accordance with Directive 2, U.S. financial institutions are prohibited from opening or maintaining a correspondent account or payable-through account for or behalf of Sberbank and from processing any transaction involving Sberbank. Directive 3 generally prohibits all transactions and dealings by U.S. persons in new debt of longer than fourteen (14) days' maturity and new equity of certain Russian financial institutions and state-owned enterprises when such new debt or equity is issued on or after March 26, 2022.

In addition to the sanctions activity of February 24, 2022 OFAC also issued several general licenses authorizing transactions that are otherwise prohibited by virtue of OFAC's SDN designations and/or Directives 2 and 3. These general licenses include:

- GL 5 authorizing certain transactions related to the business of international organizations and entities;
- GL 6 authorizing transactions ordinarily incident and necessary to the export of agricultural commodities, medicine, and medical devices to, from or transiting Russia [superseded by GL 6A issued on March 24, 2022];
- GL 7 permitting certain transactions ordinarily incident and necessary to payments and services rendered in connection with overflights of, and emergency landings in, Russia, as well as air ambulance services;
- GL 8 authorizing all transactions involving certain financial institutions (and their respective subsidiaries) that are related to energy until June 24, 2022 [superseded by GL 8B issued on April 6, 2022]
- GL 9 permitting transactions ordinarily incident and necessary to dealings in debt and equity of certain financial institutions (and their respective subsidiaries) issued prior to February 25, 2022 until May 25, 2022, provided that any divestment is made to a non-U.S. person [superseded by GL 9C issued on April 7, 2022];

- GL 10, authorizing certain transactions ordinarily incident and necessary to the winding down of derivatives contracts entered into prior to 4 PM ET on February 24, 2022 involving certain financial institutions as a counterparty or linked to the debt and equity of certain financial institutions until May 25, 2022 [superseded by GL 10C issued on April 7, 2022];

- GL 11, authorizing certain transactions ordinarily incident and necessary to the winding down of transactions involving certain financial institutions until March 26, 2022 **[EXPIRED]**; and

- GL 12, authorizing U.S. persons to reject all transactions otherwise prohibited involving certain financial institutions until March 26, 2022 **[EXPIRED]**.

On February 28, 2022, OFAC further announced the imposition of sanctions under newly issued Russia-related Directive 4, also promulgated under the aegis of Executive Order 14024. Directive 4 broadly prohibits U.S. persons from engaging in any transaction 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**, including "any transfer of assets to such entities or any foreign exchange transaction for or on behalf of such entities." In conjunction with the issuance of Russia-related Directive 4, OFAC added the three financial institutions identified in the Directive to its Non-SDN Menu-Based Sanctions ("NS-MBS") List. Subsequent to the issuance of Directive 4, OFAC issued a number of pertinent general licenses, including:

- GL 9A authorizing transactions ordinarily incident and necessary to the receipt of interest, dividend, or maturity payments in connection with the debt or equity of any Directive 4 entity issued before March 1, 2022 until May 25, 2022 [superseded by GL 9C issued April 7, 2022]; and

- GL 10A authorizing transactions ordinarily incident and necessary to the wind down of derivative contracts, repurchase agreements or reverse repurchase agreements in which any Directive 4 entity is a counterparty and entered into prior to March 1, 2022 until May 25, 2022 [superseded by GL 10C issued April 7, 2022].

- GL 13 authorizing U.S. persons to pay taxes, fees, or import duties, and purchase permits, licenses, registrations or certifications otherwise prohibited by Directive 4 through June 24, 2022; and

- GL 14 authorizing transactions with a Directive 4 entity that is otherwise prohibited by Directive 4 to the extent that the Directive 4 entity's "sole function in the transaction" is to act as an "operator" of a "clearing and settlement system" provided there is no transfer or assets to or from any Directive 4 entity and that no Directive 4 entity is either a counterparty or beneficiary to the transaction.

On March 8, 2022, President Biden issued Executive Order 14066, prohibiting the importation into the United States of Russian-origin crude oil; petroleum, petroleum fuels, oils and products of their distillation; liquefied natural gas; coal; and coal products. Executive Order 14066 also prohibits new investment in the energy sector of the Russian Federation by any U.S. person wherever located and any approval, financing, facilitation, or guarantee by a United States person, wherever located, of any transaction by a foreign person when that transaction would be prohibited if performed by a United States person.[2] In tandem with the issuance of Executive Order 14066, OFAC issued General License 16, which authorizes transactions ordinarily incident and necessary to the importation of the aforementioned goods pursuant to written contracts entered into prior to March 8, 2022 through April 22, 2022.

2. The term "new investment" was subsequently defined in corresponding guidance and represents a broad set of activities.

On March 11, 2022, President Biden also issued Executive Order 14068, prohibiting the importation into the United States of certain so-called "luxury goods" of Russian-origin. These goods include fish, seafood, and any preparations thereof; alcoholic beverages, non-industrial diamonds; and any other products of Russian-origin as may be determined by the Secretary of the Treasury, in consultation with the Secretary of State and Secretary of Commerce. Executive Order 14068 also prohibits the direct and indirect exportation, reexportation, sale, or supply of such luxury goods to any person located in Russia and any "new investment" by U.S. persons in any sector of the Russian economy as determined by the Secretary of the Treasury in consultation with the Secretary of State. Finally, Executive Order 14068 prohibits the exportation, reexportation, sale or supply of U.S. dollar-denominated banknotes to the government of Russia or any person in Russia. Simultaneous with the issuance of Executive Order 14068, OFAC issued the following related general licenses:

- GL 17 authorizing transactions ordinarily incident and necessary to the importation into the United States of fish, seafood, and any preparations thereof; alcoholic beverages; and non-industrial diamonds of Russian-origin pursuant to written contracts entered into prior to March 11, 2022 through March 25, 2022 [superseded by GL 17A issued March 24, 2022];

- GL 18 authorizing transactions ordinarily incident and necessary to the transfer of U.S. dollar-denominated banknotes in the form of noncommercial, personal remittances; and

- GL 19 authorizing transactions ordinarily incident and necessary to the personal maintenance of U.S. persons, including the payment of housing expenses, acquisition of goods or services for personal use, payment of taxes or fees, and purchase or receipt of permits, licenses, or public utility services.

On March 24, 2022, OFAC further designated dozens of Russian defense companies, hundreds of members of the Russian Duma, and the head of Sberbank as SDNs. Finally, on April 6, 2022 OFAC announced the imposition of full blocking sanctions against **Sberbank**—Russia's largest state-owned bank—and **Alfa-Bank**—Russia's largest private bank. The sanctions imposed on the financial institutions were complemented by sanctions imposed on members of Russian President Vladimir Putin's immediate family (namely, his daughters **Katerina Vladimirovna Tikhonova** and **Maria Vladimirovna Vorontsova**) as well as Foreign Minister Sergey Lavrov's family (namely, his wife **Maria Aleksandrovna Lavrova** and daughter, **Yekaterina Sergeyevna Vinokurova**). Sanctions were also imposed by OFAC on members of the Security Council of the Russian Federation for having been leaders, officials, senior executive officers or members of the board of directors of the government of Russia.

II. Trade Controls Overview

a. Background

While more recent sanctions activity in the trade controls space has focused on tightening the applicability of the Export Administration Regulations ("EAR") to Russia, the first significant action with respect to export controls was taken in the spring of 2021 by the U.S. Department of State Directorate of Defense Trade Controls ("DDTC") with respect to the export of defense articles and provision of defense services. Specifically, on March 18, 2021, DDTC amended the International Traffic in Arms Regulations ("ITAR") to incorporate Russia as a Section 126.1 country. Designation under Section 126.1 means that the United States now maintains a general policy of **denial** for any licenses or approvals to export any defense articles and services to the Russian Federation. While approvals are subject to review on a case-by-case basis, all exports of defense articles and services to Russia are generally proscribed.

Conversely, BIS has historically assumed a more restrained and measured approach to increasing Russian hostility by utilizing the Entity List and its power to require licenses for all exports bound for certain designated end-users. In July 2021, for instance, BIS added six (6) Russian entities to the Entity List based on articulable facts that the entities have been involved, are involved, or pose a significant risk of becoming involved in activities deemed contrary to the national security or foreign policy interests of the United States. These activities included undermining the conduct of U.S. elections and democratic institutions; engaging and facilitating malicious cyber activities against the United States and its allies; fostering and using transnational corruption to influence foreign governments; and violating principles of international law, including respect for the territorial integrity of independent states.

b. Recent Sanctions Activity

Beginning in February 2022, BIS began imposing restrictions on certain dual-use exports bound for export to the Russian Federation. On February 24, 2022, BIS imposed a policy of denial on the most sensitive items relied upon by the Russian Federation for the maintenance of its defense, aerospace, and maritime industries, including, but not limited to, semiconductors, computers, telecommunications hardware, information security equipment, lasers and sensors. In addition, BIS added forty-nine (49) Russian entities to the Entity List with an expanded license requirement for all items subject to the EAR (including foreign-produced items subject to the Russia Military End User Foreign Direct Product rules). Finally, BIS imposed comprehensive export, reexport and transfer (in-country) restrictions on the so-called Donetsk People's Republic ("DNR") and Luhansk People's Republic ("LNR") regions of Ukraine.

On March 2, 2022, BIS imposed new license requirements and review policies on Belarus for certain items under the EAR. These changes effectively rendered Belarus subject to the same sanctions that were imposed on Russia under the EAR effective February 24, 2022. Specifically, BIS imposed new Commerce Control List ("CCL")-based license requirements for exports bound for Belarus; expanded the applicability of the foreign direct product rules to make them applicable to Belarusian military end users; and set forth a review policy of denial as to all license requirements imposed by the March 2, 2022 EAR modifications. BIS further constrained the ability of prospective exporters to utilize the EAR's license exceptions with respect to a variety of commodities.

On March 4, 2022, BIS expanded restrictions imposed on exports related to Russian deepwater oil and gas exploration and extraction. Specifically, BIS imposed a license review policy of denial with respect to all such exports and similar restrictions on items used to refine oil. In announcing its actions, BIS specifically noted that it was acting to limit Russia's ability to raise revenue from the sale of refined oil products, including gasoline, that enables Russia to fund its military efforts. In concert with the new policy, BIS also added ninety-one (91) new parties to the Commerce Department's Entity List based upon a determination that the entities were involved, contributed to, or provided other support for the Russian security services, military and defense sectors, and research and development efforts.

On March 11, 2022, BIS implemented a pair of rules designed to restrict the exportation of specified "luxury goods" to Russia and Belarus generally, as well as to Russia and Belarusian oligarchs specifically. Pursuant to the new rule, BIS imposed licensing requirements on all luxury goods subject to the EAR that are destined for Russia and Belarus. It further imposed a licensing requirement on all luxury goods destined for export to Russian and Belarussian "oligarchs and malign actors" regardless of geographic location. Under both of the new license requirements—codified at 746.10.(a)(1) and (2) of the EAR, respectively—a policy of denial now applies.

In late March 2022, BIS also acted to identify commercial and private aircraft exported to Russia in violation of U.S. export controls. In a pair of announcements released on March 18, 2022 and March 30, 2022, BIS publicly identified certain aircraft involved in an apparent violation of the EAR to "notify all persons and companies in the United States and abroad that providing any form of service to these aircraft may constitute a violation of the EAR." Among the more notable private aircraft implicated in export violations was a privately-owned and operated Gulfstream G650ER owned by Russian billionaire and Putin confidant Roman Abramovich.

On April 1, 2022, BIS added an additional one hundred twenty (120) entities in Russia and Belarus to the Commerce Department's Entity List. The entities were added to the Entity List for both supporting and enabling support of Russia's invasion of Ukraine, and for attempting to acquire items subject to the EAR in support of Russian and Belarussian military forces. This action was followed by an April 7, 2022 announcement of enforcement actions against three (3) Russian airlines that operated aircraft in apparent violation of U.S. export controls. Specifically, BIS alleged that Russian-based carriers **Aeroflot**, **Azur Air**, and **UTAir** operated international flights into Russia for which export authorizations were required. As a consequence of their actions, BIS issued temporary denial orders ("TDOs") to each airline depriving them of the right to participate in any transactions subject to the EAR, including exports and reexports from the United States. The TDOs were issued for an initial period of one hundred eighty (180) days and are subject to renewal.

Finally, on April 9, 2022, BIS announced sweeping new restrictions on **all exports** to Russia and Belarus in response to ongoing aggression in Ukraine. Pursuant to the April 9, 2022 announcement, licenses are now required for **all items** designated on the CCL (Categories 0-9) when intended for export to Russia and/or Belarus. In addition, BIS expanded the applicability of the new FDP rules for Russia and Belarus and to Russian/Belarussian Military End Users to all items on the CCL. With limited exceptions, applications involving such CCL items are subject to a license review policy of denial. BIS's April 9, 2022 announcement is the single most aggressive stride taken by the U.S. government to punish Russia for its aggression towards Ukraine. Short of a full embargo, these new license requirements will have a crippling effect on Russia's ability to obtain critical commodities needed to continue its Ukraine incursion.

III. The Bottom Line

The ongoing conflict in Ukraine poses a unique set of challenges for legal and compliance professionals tasked with ensuring that an organization is compliant with sanctions that are seemingly ever-changing. Despite this challenge, however, legal and compliance professionals are cautioned to return to the basics when considering how best to devise and implement internal controls sufficient to detect and deter potential legal violations. Here, it seems trite but necessary to mention that a foundational element of a sound compliance risk mitigation strategy is a dynamic risk assessment process. Accordingly, organizations are encouraged to revisit their risk assessments in painstaking detail to adequately pinpoint and address any risks associated with exposure to Russia, Belarus, and Ukraine generally.

Second, organizations are encouraged to utilize the tools likely already at its disposal—including continuous screening against government watchlists—as a first line of defense against a potential infraction. Because entities and individuals are frequently being added to such watchlists—including but not limited to OFAC's SDN list—it is imperative that the organization screen and rescreen all individuals with Russian, Belarusian or Ukrainian ties.

Finally, organizations are advised to tackle the challenge of implementing sanctions controls piecemeal and in accordance with their risk profile rather than wholesale. In line with both industry best practice and regulator guidance, this means aligning the organization's sanctions implementation strategy with its risk profile to avoid addressing elements of sanctions regulations that simply have no bearing on the organization's activities. If, for instance, the organization does not engage in the provision of any goods or services to customers in Russia, then it makes very little sense to implement controls to address purely theoretical risks. Put simply, aggressive action is required only to the extent a tangible risk exists. By resorting to the foundational tools of legal and compliance professionals generally, organizations can ensure that they rise to meet the challenge of a dynamic regulatory climate with the right focus and resources.

IV. Looking Forward

The decision of the United States and its allies to swiftly implement aggressive sanctions against Russia for its violation of international norms proscribing the invasion of a sovereign nation is unprecedented from both an implementation and enforcement standpoint.

From an implementation perspective, the decision to promulgate progressively more severe economic and trade sanctions against Russia is a critical test of the U.S. government's ability to keep pace with constantly evolving geopolitical circumstances, competently assess the threat posed by Russian actors and institutions, and respond in a fashion that maximizes the economic pressure exerted on the Putin regime. More significantly, the decision of the U.S. government to aggressively enforce Russia sanctions *ab initio* while providing no time for industry to acclimate to the new sanctions regulations is a sign of how dire the current political circumstances are. Given the fact that the DOJ has publicly prioritized the enforcement of Russian sanctions regulations against prospective violators, all organizations are cautioned to take proactive measures now to implement controls designed to mitigate the potential for any infraction. Organizations are further cautioned to meticulously document their mitigation activities to demonstrate to regulators that their sanctions compliance program is both risk-based and dynamic. In the Russian sanctions context, as the old adage famously goes, "an ounce of prevention is worth a pound of cure."

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