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US Sanctions Tighten on Russia's Financial Sector and Technology Imports

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What Happened:

On February 28, 2022, the US Department of Treasury's Office of Foreign Assets Control ("OFAC") issued further sanctions on Russia's Central Bank, National Wealth Fund, and Ministry of Finance, and announced regulations to implement Executive Order 14024 under the Russia Harmful Foreign Activities Sanctions Program. On February 24, 2022, the Department of Commerce's Bureau of Industry and Security ("BIS") issued an immediate final rule implementing sanctions under the Export Administration Regulations ("EAR").[1]

The Bottom Line:

US sanctions on Russia have continued to escalate in response to Russia's invasion of Ukraine by targeting Russian banks' ability to manage the economic fallout of sanctions and limiting access to technology vital to Russia's defense, aerospace, and maritime industries. The stated purpose of the most recent round of economic sanctions is to impose measures to ensure Russia cannot use its Central Bank reserves to support its currency and thereby undermine the impact of prior sanctions.[2] The latest sanctions broadly prohibit all transactions with Russia's Central Bank, National Wealth Fund, and Ministry of Finance. BIS's February 24 final rule broadens export controls primarily targeting Russia's defense, aerospace, and maritime sectors, with the intention of restricting Russia's access to vital technological inputs key to its military-industrial base.[3]

The Full Story:

Following Russia's recognition of break-away regions in Eastern Ukraine on February 21, 2022, the United States responded with a number of economic sanctions including, among other things, prohibitions on participating in certain transactions involving bonds issued 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. On February 24, 2022, OFAC announced more expansive sanctions on Russia in response to Russia's military escalation into a full-scale invasion of Ukraine. Our team described these sanctions in prior client alerts available here and here.

Also on February 24, 2022, BIS issued its first export sanctions in response to the invasion under the

EAR. On February 28, 2022, OFAC issued Directive 4 (the "Russia-related Sovereign Transactions Directive")[4] further restricting transactions with Russia's Central Bank, National Wealth Fund, and Ministry of Finance, and designated a number of Russia's key sovereign wealth funds as Specially Designated Nationals ("SDNs"). On that same day, OFAC announced new regulations to implement the expanded Russian Harmful Foreign Activities Program.

OFAC's Russia-related Sovereign Transactions Directive and Blocking Sanctions

OFAC's Russia-related Sovereign Transactions Directive broadly prohibits US persons from engaging in any transaction involving Russia's Central Bank, National Wealth Fund, and Ministry of Finance. Prohibited transactions include the transfer of assets to these entities or foreign exchange transactions for or on their behalf. Notably, OFAC's Russia-related Sovereign Transactions Directive is a non-SDN sanction—while US persons are prohibited from transactions with the three entities subject to the Directive, the property of Russia's Central Bank, National Wealth Fund, or Ministry of Finance has not yet been fully blocked by OFAC.

Simultaneous with issuance of the Russia-related Sovereign Transactions Directive, OFAC issued a General License authorizing transactions related to energy with certain Russian banks. Russia-related General License 8A, which replaces and supersedes General License 8 (issued with the February 24, 2022, tranche of sanctions on Russian banks), includes Russia's Central Bank among the list of banks with which US persons may engage in transactions related to energy until June 24, 2022.[5]

OFAC also issued full blocking sanctions on three of Russia's key sovereign wealth funds: Russian Direct Investment Fund ("RDIF"), Joint Stock Company Management Company of the Russian Direct Investment Fund ("JSC RDIF"), and Limited Liability Company RVC Management Company ("LLC RVC"). These funds have been added to OFAC's SDN list and all property or interest in property of the funds held by US persons or within the United States is effectively frozen.

Notably, these sanctions are effective immediately and do not have a thirty-day wind-down period like many of the other recent sanctions measures.

OFAC Announces Regulations to Implement the Russian Harmful Foreign Activities Sanctions Program

On February 28, 2022, OFAC announced regulations implementing the Russian Harmful Activities Program that go into effect on March 1, 2022.[6] The regulations provide clarity on the application of defined terms, OFAC's 50 percent rule, blocked accounts, reporting, and enforcement penalties guidance for the sanctions program, which has expanded rapidly over the last several days. The regulations are generally consistent with regulations issued by OFAC to implement other sanctions programs and OFAC intends to issue more comprehensive regulations in the near future.

Sanctions on Russian President Vladimir Putin and Others

On February 25, 2022, OFAC imposed sanctions on the President of the Russian Federation, Vladimir Putin, and the Minister of Foreign Affairs, Sergei Lavrov, as well as other members of Russia's Security Council, by designating them as SDNs. As noted in a press release by the government, "It is exceedingly rare for Treasury to designate a head of state; President Putin joins a very small group that includes despots such as Kim Jong Un, Alyaksandr Lukashenka, and Bashar al-Assad."[7]

As a result of these designations, all property and interests in property of the designated individuals that are in the United States or in the possession or control of US persons are blocked and must be reported to OFAC. In addition, any entities that are owned, directly or indirectly, 50 percent or more by one or more blocked persons are also blocked. All transactions by US persons or within (or transiting) the United States that involve any property or interests in property of designated or otherwise blocked persons are prohibited unless authorized by a general or specific license issued by OFAC, or otherwise exempt. These prohibitions include the making of any contribution or provision of funds, goods, or services by, to, or for the benefit of any blocked person and the receipt of any contribution or provision of funds, goods, or services from any such person.

The White House has announced that it will work with other nations to form a task force to seek out, identify, and freeze the assets of Russian SDNs held offshore or in a manner that otherwise obscures ownership in an effort to limit the ability of Vladimir Putin and others to evade sanctions.

BIS Export Control Sanctions

The BIS final rule establishing export control sanctions in response to the Ukrainian invasion implements new Russia license requirements and licensing policies. It builds on existing restrictions on exports to Russia and implements the following major policies specific to Russia and Russian end-users through the following:

- Expands licensing requirements across Categories 3-9 of the Commerce Control List ("CCL"), including on 58 different Export Control Classification Numbers ("ECCNs") for items that did not previously require a license to export to Russia. These items include microelectronics, telecommunications items, sensors, navigation equipment, avionics, marine equipment, and aircraft components.

- Implements a policy of denial making it significantly more difficult to get any license to export items to Russia. That policy requires a case-by-case review of Russian license applications with limited exemptions.

- Expands military end use restrictions on nearly all items subject to EAR, whether or not listed on the CCL.

- Creates a new Foreign Direct Product Rule ("FDPR") specific to Russia and Russian military end users that expands export controls to foreign produced products. The FDPR restricts the export to Russia and Russian military end users of foreign-produced items that are (1) the direct product of US-origin software or technology or that are produced by plants or (2) major components that are the direct product of US-origin software or technology.

- Significantly restricts the use of EAR license exceptions for Russia exports, reexports and in-country transfers.

- Applies Entity List restrictions to 49 Russian entities, meaning a license to export any item subject to the EAR, whether or not listed on the CCL, will be required to export to these entities.

Additional Sanctions Continue to Be Forthcoming:

The White House has signaled that further sanctions against Russia will be forthcoming should Russia continue its assault on Ukraine. Such additional sanctions may entail further full blocking sanctions against additional Russian banks and designation of additional individuals, as well as further restrictions on trade with Russia.

In addition to the sanctions imposed by the United States, other authorities, including the European Union, the United Kingdom, and Japan, have imposed sanctions on Russia. The White House has announced that, in coordination with US officials, authorities in the European Union will implement a regulation that removes certain Russian banks from the SWIFT international payments network, effectively shutting them out of the world's financial systems, following the model used to disconnect Iranian banks from SWIFT in 2012. US persons and companies doing business, directly or indirectly, in Russia, Belarus, or Ukraine should review sanctions exposure carefully and deploy sufficient compliance controls to limit sanctions risk and plan for disruptions to banking transactions involving Russian banks. Non-US individuals and companies should also be aware of applicable sanctions regimes, and the authority of OFAC to sanction non-US persons and companies engaged in activities that would be prohibited by a US person in certain circumstances, and should similarly review their sanctions exposure carefully and adopt appropriate policies.

FOOTNOTES

[1] Final Rule, Implementation of Sanctions Against Russia Under the Export Administration Regulations (Feb. 24, 2022), https://public-inspection.federalregister.gov/2022-04300.pdf.

[2] White House, Press Briefing, *Background Press Call by a Senior Administration Official on Imposing Additional Severe Costs on Russia* (Feb. 26, 2022), https://www.whitehouse.gov/briefing-room/press-briefings/2022/02/27/background-press-call-by-a-senior-administration-official-on-imposing-additional-severe-costs-on-russia/.

[3] US Dept. of Commerce, Press Release, *Commerce Implements Sweeping Restrictions on Exports to Russia in Response to Further Invasion of Ukraine* (Feb. 24, 2022), https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/2914-2022-02-24-bis-russia-rule-press-release-and-tweets-final/file.

[4] OFAC, Directive 4, Prohibitions Related to Transactions Involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, and the Ministry of Finance of the Russian Federation (Feb. 28, 2022), https://home.treasury.gov/system/files/126/eo14024_directive_4_02282022.pdf.

[5] Russia-related General License No. 8A, Authorizing Transactions Related to Energy (Feb. 28, 2022), https://home.treasury.gov/system/files/126/russia_gl8a_1.pdf.

[6] OFAC, Press Release, *Issuance of Russian Harmful Foreign Activities Sanctions Regulations* (Feb. 28, 2022), https://home.treasury.gov/policy-issues/financial-sanctions/recent-actions/20220228_33.

[7] US Department of the Treasury, Press Release, *US Treasury Imposes Sanctions on Russian Federation President Vladimir Putin and Minister of Foreign Affairs Sergei Lavrov* (Feb. 25, 2022), https://home.treasury.gov/news/press-releases/jy0610.

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