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New Russian Sanctions Signal Paradigm Shift

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Britt Mosman is a partner in and Vice-Chair of the Global Trade & Investment Practice Group in Washington, who advises clients on a wide range of international transactional, compliance, and enforcement issues. Her experience includes advising global financial institutions and leading multinational companies on economic sanctions, Bank Secrecy Act (BSA) / anti-money laundering (AML), and export controls laws, as well as transaction reviews by the Committee on Foreign Investment in the United States (CFIUS) and other national security-related issues. In addition, as part of the Willkie Digital Works team, Britt routinely advises crypto sector participants on how to comply with BSA/AML and economic sanctions requirements.

William J. Stellmach

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William is a Partner in Willkie's Washington, D.C. office and Co-Chair of the firm's White Collar Defense Group, where he leads one of the premier compliance, investigations and enforcement defense practices in United States. He is a distinguished former federal prosecutor and regulator, and previously served as head of the Fraud Section of the U.S. Department of Justice's Criminal Division as well as in the Division of Enforcement at the Securities and Exchange Commission. Drawing on a unique range of experience, he regularly represents a broad range of companies, financial institutions and their executives in matters involving securities fraud, foreign bribery, sanctions, antitrust, cybersecurity, insider trading and money laundering. He also has extensive experience representing corporations and individuals outside the United States in responding to inquiries and investigations.

Sean Sandoloski
Counsel, Litigation

Sean Sandoloski serves as Counsel in the firm's Litigation Department. Sean previously worked in government, advising the Executive Branch on a range of matters, including litigation and policy initiatives, and serving in the Appellate Section of the Department of Justice's Antitrust Division. His practice focuses on government investigations, including those undertaken by Congress, as well as tackling complex legal issues and appeals. Leveraging his experience in government—as well as representing clients before the full spectrum of government authorities and at every level of the federal judiciary—Sean focuses on providing holistic solutions to clients' complex problems. His multidisciplinary approach enables him to successfully tackle high-stakes, fast-moving issues, and to advise clients on strategic and regulatory matters. Additionally, Sean has extensive experience in administrative and antitrust law and litigation.

Joshua Nelson

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Joshua Nelson is an associate in Willkie's global trade and investment group in Washington, DC. Joshua provides advice to both domestic and foreign clients on government regulation of international trade and investment, particularly with regard to economic sanctions, export controls, and the Committee on Foreign Investment in the United States.

Program

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Overview of Russia Sanctions

Comprehensive Sanctions

- At the time of Russia's invasion of Ukraine, President Putin announced his recognition of the Donetsk and Luhansk People's Republics as "independent" states.

- As an initial response, President Biden signed an Executive Order ("E.O.") imposing comprehensive sanctions on the so-called Donetsk People's Republic and Luhansk People's Republic on February 21, 2022. Along with Crimea, these sanctions are likely to continue for the duration of Russia's occupation of these territories.

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Russian Financial Institutions

- The United States has implemented sanctions that affect many aspects of the Russian financial system. Numerous significant Russian banks have been sanctioned, preventing U.S. persons from engaging in any activities with them.
- Moreover, certain banks have been subject to debt and equity restrictions that prevent them from raising funds under Directive 3 to E.O. 14024.
- The United States has also restricted the ability of the Russian government to raise funds, through restrictions on sovereign debt, and transactions with government financial institutions under Directive 1A to E.O. 14024

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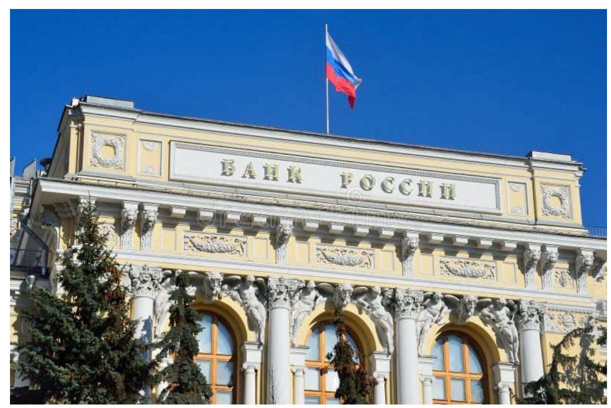

Energy-Related Sanctions

- The United States, in partnership with other G7 countries, implemented a price cap for the provision of certain services ("Covered Services") related to the maritime transport of Russian oil and petroleum products.
- U.S. persons are prohibited from providing Covered Services as they relate to the maritime transport of Russian oil and petroleum products unless the oil or petroleum products were purchased at or below the price cap.
- In recent months, OFAC has begun to sanction third country service providers that have transported oil in violation of the price cap. We expect the price cap and related enforcement to continue to be a major focus for OFAC.

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Sectoral Sanctions

- Throughout the course of the Ukraine conflict, the United States has identified specific industries that have proven important to the Russian war effort. Within those industries, OFAC has been empowered to identify and designate specific individuals and entities ("**persons**") that have contributed to the conflict.

- E.O. 14024 Section 1(a)(i) authorizes the Secretary of the Treasury to determine specific sectors of the Russian economy as a basis for blocking actors who are contributing to Russia's war in Ukraine, in some cases with direct support to Russia's government or military or due to their strategic or financial importance for the Russian economy.

- Once OFAC determines E.O. 14024 shall apply to a sector of the Russian economy, it may then designate persons who operate or have operated in that sector.

Sanctions Targeting Evasion

- The U.S. sanctions response has had a significant impact on Russia. Russian intelligence services have been directed to find channels for evasion and backfilling.
- OFAC sanctioned members of Russia's Federal Security Bureau on June 27, 2022, for establishing a covert procurement network to secure electronics for Russia's defense industry. OFAC designated several other individuals and entities identified in sanctions evasion schemes on September 30, 2022.
- The United States has identified and imposed sanctions on a number of non-Russian nationals for enabling Russian military activity and engaging in sanctions evasion efforts.
- The United States has indicated that enforcement of Russia sanctions will increase in 2024.

Executive Order 14114: A Warning to Non-U.S. Banks

Executive Order 14114

- On December 22, 2023, President Biden signed E.O. 14114, authorizing additional sanctions related to Russia's harmful foreign activities in Ukraine.

- Chief among these new sanctions authorities is an amendment to E.O. 14024, authorizing "secondary" sanctions against foreign financial institutions ("FFIs") that conduct or facilitate significant transactions in support of Russian harmful foreign activities.

- Importantly, these new sanctions are authorized without regard to whether the FFI has knowledge that they are conducting or facilitating such a transaction.

- E.O. 14114 also expands the import restrictions of E.O. 14068 to include additional fish, seafood, diamond, and gold products, that are prohibited from entering the United States and its foreign trade zones.

Secondary Sanctions on FFIs

- E.O. 14114 authorizes the imposition of secondary sanctions against FFIs determined to have:
  - Conducted or facilitated any **significant transaction** or transactions **for or on behalf of any person designated** . . . for operating or having operated in the technology, defense and related materiel, construction, aerospace, or manufacturing sectors of the Russian Federation economy, or other such sectors as may be determined to support Russia's military-industrial base; or
  - Conducted or facilitated any **significant transaction** or transactions, or provided **any service**, involving **Russia's military-industrial base**, including the sale, supply, or transfer, directly or indirectly, to the Russian Federation of any item or class of items as may be determined [by Treasury in consultation with other agencies].
- E.O. 14114 authorizes two types of sanctions: (1) blocking, and (2) correspondent account sanctions

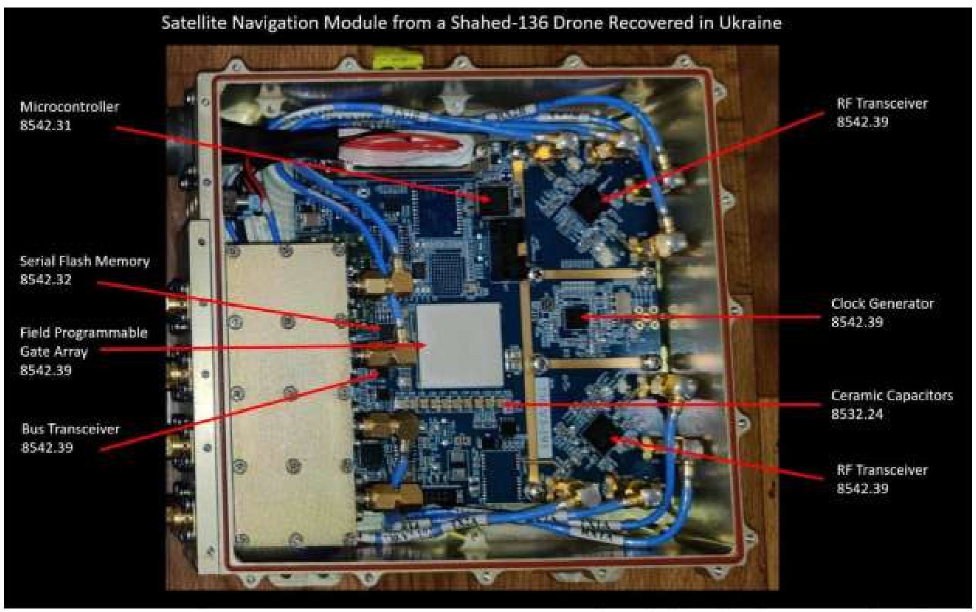
Prong One: Transactions with Certain SDNs

- The first prong targets FFIs that engage in significant transaction(s) with certain SDNs, namely persons operating in identified sectors.
- The Secretary of the Treasury may designate additional sectors as supporting the Russian military-industrial base, which would authorize sanctions against FFIs.
- OFAC has stated that it intends to update the SDN List to make clear in which sector a person was designated for operating. Currently, the best way to verify the relevant sector is to cross-reference the relevant OFAC press release, which identifies the sector.

Prong Two: Military-Industrial Base

- Prong two more broadly authorizes the imposition of sanctions, even where there is no blocked person involved.

- OFAC has stated in guidance (FAQ 1151) that Russia's military-industrial base includes the technology, defense and related material, construction, aerospace, and manufacturing sectors – the same sectors relevant to Category One. Likewise, OFAC may expand this to include other sectors.



- OFAC has issued a determination identifying the certain goods in the following categories as relevant to the "sale, supply, or transfer" clause, with a total of 29 unique items.

No Knowledge Qualifier

- Unlike prior authorities, the secondary sanctions authorized by E.O. 14114 do not include a knowledge qualifier.
- Easier for OFAC to target FFIs.
- FFIs should conduct appropriate diligence on their customers and transactions to ensure they are not operating in the sectors described above, as the government need not show that an FFI had knowledge that a transaction related to these sectors to impose sanctions on the FFI.

Sanctions or Other Restrictive Measures

- E.O. 14114 authorizes designation to the SDN List, or imposition of restrictions/closure of correspondent accounts in the United States.

- Two banks have had correspondent accounts closed under similar secondary sanctions authorities in the past:
  - Bank of Kunlun (China)
  - Elaf Bank (Iraq)

- Both banks were sanctioned in July 2012 for knowingly facilitating significant transactions and providing significant financial services for designated Iranian banks.

Enforcement

Enforcement

- In addition to the risk of designation or correspondent account restrictions, FFIs should be aware of the risk of a civil or criminal enforcement action if directly subject to U.S. jurisdiction.
- OFAC has jurisdiction over civil penalties for sanctions violations.
- The Department of Justice, National Security Division ("NSD") has jurisdiction over criminal penalties for sanctions violations.
- Recent compliance notes and other guidance from OFAC and NSD emphasize the importance of considering voluntary self-disclosures ("VSDs") to *both* OFAC and NSD to mitigate penalty risk

Civil Penalties (OFAC)

- For civil penalties the total penalties vary based on the sanctions program underlying the offense, the egregiousness of the offense, whether the offense was voluntarily self-disclosed, and some other mitigating/ aggravating factors.

OFAC

- The actual penalty can be significantly reduced by filing a voluntary self-disclosure and the presence of various mitigating factors, including a well-developed compliance system based on risk management.

- Under OFAC Guidelines Section II.G.1., OFAC may withhold, deny, suspend, modify, or revoke an OFAC-issued license in response to violations of U.S. sanctions.

Criminal Penalties (DOJ NSD)

- Criminal penalties are generally reserved for willful and malicious attempts to violate U.S. sanctions, and are enforced by NSD.

- Penalties are based on the underlying statute at issue.

- NSD has stated that voluntarily self-disclosed offenses (with full cooperation and remediation) will be treated under a presumption that the company will receive a non-prosecution agreement and will be forced to surrender any gains obtained from the underlying conduct.

- In order to receive credit for a voluntary disclosure to NSD, the disclosure must be made prior to an imminent threat of disclosure or government investigation.

Criminal Penalties (DOJ NSD)

- DOJ has recently been talking tough about sanctions enforcement
  - “Leave no stone unturned” – AG Merrick Garland
  - “New level of intensity and commitment to sanctions enforcement” – DAG Lisa Monaco
  - “Sanctions are the new FCPA”

- DOJ has put its money where its mouth is, hiring ~25 new prosecutors focused on sanctions and expert control violations
  - Chief Counsel for Corporate Enforcement in NSD

- Characteristics of Criminal Cases

Voluntary Self Disclosures

- NSD has stated that a disclosure to OFAC or another regulatory agency <u>will not qualify</u> as a voluntary disclosure to NSD.

- Accordingly, it is important to analyze whether a violation involves willful conduct such that it may be referred to NSD by a civil enforcement authority and carefully consider how best to sequence multiple disclosures to multiple agencies.

- OFAC has stated similarly that voluntary self-disclosure to another government agency (but not to OFAC) <u>may</u> be considered a voluntary self-disclosure by OFAC based on a <u>case-by-case assessment</u>.

- A business considering voluntary disclosure of a potential sanctions violation should consider submitting disclosures to OFAC and NSD.

Tri-Seal Compliance Notices

- In March and July of 2023, DOJ, Treasury, and Commerce have released joint notices regarding sanctions and export controls.

- Underscore an enhanced level of cooperation and coordination among the bodies responsible for enforcing national security-related trade compliance laws.

- Topics have included effective compliance programs and VSD Policies.

Task Force KleptoCapture

- Task Force KleptoCapture is a unit in the Office of the Deputy Attorney General dedicated to enforcing sanctions, export restrictions, and other economic countermeasures against Russia.

- Notable enforcement action by the Task Force includes seizure of six properties and the superyacht Amadea, owned by Russian oligarch Suleiman Kerimov.

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REPO Task Force

- The Department of Justice and OFAC similarly cooperate on the Russian Elites, Proxies, and Oligarchs (REPO) Task Force.
- The REPO Task Force is an international effort involving Australia, Canada, France, Germany, Italy, Japan, United Kingdom, United States, and European Commission.
- Since the Task Force was established in March 2022, it has blocked or frozen more than $58 billion in assets, including oligarchs' planes, yachts, and property.

Compliance Takeaways

OFAC Guidance

- Concurrently with the Order, OFAC issued guidance recommending that FFIs mitigate the risk of secondary sanctions under the Order by reviewing their customer bases, communicating expectations to customers, using questionnaires for exporter clients, and obtaining attestations from clients that they are not engaging in prohibited activity, among other things.

- At the same time, OFAC guidance reminds FFIs that there remains broad authorization for transactions otherwise prohibited by E.O. 14024

- OFAC therefore encourages FFIs to strike a balance between de-risking, by halting Russia-related transactions entirely, and wholesale support of Russia.

Questions?

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