

New Ukraine-Russia Sanctions Raise Compliance Issues

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The Obama Administration yesterday significantly expanded the economic sanctions that President Obama imposed in March in response to the ongoing crisis in Ukraine.

First, while President Obama had previously raised the possibility of sanctions targeting key sectors of the Russian economy, the Administration exercised that power yesterday for the first time. Specifically, the Administration has targeted two major Russian banks (Gazprombank and VEB, the bank for development and foreign economic affairs) and two major Russian energy companies (Rosneft and Novatek). The new sanctions are intended to prevent the targeted companies from raising capital through new debt or equity offerings in the U.S. or with the assistance of U.S. persons anywhere in the world. In addition, the new restrictions are likely to affect many trade transactions involving Russia.

The new sectoral sanctions seem to be designed both to put economic pressure directly on the four targeted companies and also to signal to Russia the prospect that more Russian companies will be excluded from the U.S. capital markets, whether in banking, energy, or other sectors. They also signal that the Administration may unveil other new types of sectoral sanctions, up to the maximum possibility of prohibiting U.S. persons from doing any business whatsoever with targeted sectors of the Russian economy. Yesterday's actions therefore represent a continuation of the Administration's apparent strategy of expanding sanctions gradually while flagging the possibility of more stringent actions if Russia continues its current policies in Ukraine.

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These new sanctions will raise compliance challenges for U.S. companies, especially U.S. financial institutions. The Office of Foreign Assets Control (OFAC) has already recognized and attempted to ameliorate these challenges by publishing a general license authorizing U.S. persons to engage in certain transactions involving derivatives connected with securities of the targeted companies. OFAC also announced that the capital-markets restrictions apply not only to the named companies, but also to new securities issued by their majority-owned subsidiaries, raising diligence challenges that have already proved difficult for U.S. companies doing business in Russia. Even at the most basic level, U.S. persons should update their compliance systems to account for OFAC's publication of a new "Sectoral Sanctions Identifications List," the names of which do not appear on OFAC's SDN List, a comprehensive listing of individuals and entities whose property is blocked and with whom U.S. persons cannot do business of any kind.

Second, OFAC yesterday added some names to the SDN List, blocking the assets of several persons, including eight Russian arms companies (notably including weapons manufacturer Kalashnikov), a shipping facility in Crimea, two secessionist groups in Ukraine, and a number of individuals in Russia and Ukraine.

These new sanctions may continue to evolve. We encourage clients to keep a close eye on the news, including new types of sanctions, new targets for the sanctions, sanctions imposed by the European Union and other countries, and Russian retaliatory actions.