ALERTS

Escalating U.S.–Russia Tensions Lead to New Sanctions, Heightened AML Risks

April 4, 2014

The United States and others have imposed economic sanctions and issued anti-money laundering advisories in the wake of the growing political tensions between the United States and Russia over the fate of Ukraine. This *Alert* summarizes the actions taken by authorities to date and discusses compliance implications for U.S. businesses engaged in transactions with Russian or Ukrainian counterparties. Firms are advised to continue monitoring developments in this rapidly fluctuating area of heightened sanctions and AML risk.

Sanctions by the United States

Russia's actions in Crimea have been met with a series of Ukraine-related sanctions by the United States, including three Executive Orders and the addition of dozens of names to the list of Specially Designated Nationals and Blocked Persons ("SDN List") maintained by the U.S. Treasury Department's Office of Foreign Assets Control ("OFAC").[1]

These new sanctions, issued principally under the authority of the International Emergency Economic Powers Act ("IEEPA"), apply to all United States persons, including all U.S. citizens and permanent resident aliens regardless of where they are located, all persons and entities within the United States, and all U.S. incorporated entities and their foreign branches ("U.S. persons"). In all three Executive Orders, President Obama authorizes the Secretary of Treasury, in consultation with the Secretary of State, to determine whether persons (defined as individuals or entities) fall under specified categories (set forth below) leading to their designation as SDNs. U.S. persons are prohibited from dealing with SDNs wherever they are located and all SDN assets are blocked. Further, any transaction that

Copyright © 2024 Schulte Roth & Zabel LLP

Attorney Advertising

evades or avoids the prohibitions of the three Executive Orders constitutes a violation thereof. The three Executive Orders also deny immigrant and nonimmigrant entry into the United States of persons on the SDN List.

- *Executive Order 13660 of March 6, 2014.*President Obama declared a national emergency and prohibited dealings with individuals or entities determined by the Secretary of Treasury: (i) to be responsible for or complicit in, or to have engaged in, directly or indirectly, actions or policies undermining the democracy or territorial integrity of Ukraine, or the misappropriation of Ukrainian state assets; (ii) to have asserted governmental authority over any part or region of Ukraine without authorization of the Government of Ukraine; (iii) to be a leader of an entity involved in the foregoing activities or an entity with blocked property; (iv) to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services to or in support of, the foregoing activities or any person with blocked property; or (v) to be owned or controlled by, or have acted for or on behalf of, directly or indirectly, any person with blocked property.
    - Pursuant to Executive Order 13660, four individuals, including two former Ukrainian government officials and two Crimean separatist leaders, have been designated as SDNs.
- *Executive Order 13661 of March 16, 2014.*President Obama identified as additional prohibited individuals or entities those determined by the Secretary of Treasury: (i) to be an official of the Government of the Russian Federation ("Russia");[2] (ii) to operate in the arms or related materiel sector in Russia; (iii) to be owned or controlled by, or act for or on behalf of, directly or indirectly, a senior Russian government official or a person with blocked property; or (iv) to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services to or in support of, a senior Russian government official or a person with blocked property.
    - Pursuant to Executive Order 13661, 27 individuals and one entity have been designated as SDNs. Among them are 23 Russian government officials, including high-ranking executive branch officials, legislators, presidential aides and the Chairman of Russian Railways, a state-owned company.[3] Also named are four leading Russian businessmen with close ties to President Vladimir V. Putin: Gennady Timchenko, a founder of Gunvor, an oil and energy commodity trading company in which Putin is alleged to have investments; Arkady and Boris Rotenberg,

Copyright © 2024 Schulte Roth & Zabel LLP
Attorney Advertising

brothers who are said to have made billions of dollars in contracts awarded to them by Putin for the Sochi Winter Olympics and Gazprom, the state-owned oil company; and Yuri Kovalchuk, the largest shareholder of Bank Rossiya, whom the United States says acts as the personal banker for Putin and other senior Russian officials. Bank Rossiya was also added to the SDN List.[4]

- *Executive Order 13662 of March 20, 2014.* President Obama identified as additional prohibited individuals or entities those determined by the Secretary of Treasury: (i) to operate in designated sectors of the Russian economy, such as financial services, energy, metals and mining, engineering, defense and related materiel; (ii) to have materially assisted, sponsored, or provided financial, material, or technological support for, or goods or services to or in support of, any person with blocked property; or (iii) to be owned or controlled by, or have acted for or on behalf of, directly or indirectly, any person with blocked property.
    - To date, no individuals or entities have been designated as SDNs pursuant to Executive Order 13662. However, inasmuch as this Executive Order is directed at key Russian industries such as the financial services, energy and defense sectors, it has the potential of leading to prohibitions that will have an even greater impact on business transactions.

The fact that an individual or entity falls within one of the categories listed in the Executive Orders (e.g., is a Russian government official or operates in the Russian financial services industry) does not itself render the individual or entity an SDN with whom U.S. persons are prohibited from dealing. Such an individual or entity becomes an SDN only if and when designated as such by the Secretary of Treasury.

Sanctions by the European Union and Others

The European Union adopted Council Decision 2014/119/CFSP and Regulation 208/2014 on March 5, 2014, sanctions which freeze all funds and economic resources belonging to, owned, held or controlled by persons identified as responsible for the misappropriation of Ukrainian State funds and persons responsible for human rights violations in Ukraine.[5] The European Union adopted Council Decision 2014/145/CFSP and Regulation 269/2014 on March 17, 2014, and an implementing decision and regulation on March 21, 2014, sanctions which restrict travel and freeze all funds and economic resources belonging to,

Copyright © 2024 Schulte Roth & Zabel LLP
Attorney Advertising

owned, held or controlled by persons responsible for actions which undermine or threaten the territorial integrity, sovereignty and independence of Ukraine.[6] While there is substantial overlap between the EU and U.S. sanctions, the EU sanctions reach additional individuals not named as SDNs by the United States. Nations around the world are imposing similar Ukrainian-related sanctions, including Australia, Canada, Norway and the United Kingdom.

Ukraine AML Advisories

The U.S. Treasury Department's Financial Crimes Enforcement Network ("FinCEN") has issued two advisories warning financial institutions of heightened money laundering risks relating to the crisis in the Ukraine. FIN-2014-A001 was issued on Feb. 25, 2014, reminding financial institutions that they are required to apply enhanced scrutiny to private banking accounts held by or on behalf of senior foreign political figures and to monitor transactions that could represent misappropriated or diverted state assets, the proceeds of bribery or corruption, or other illegal payments, especially with respect to potentially suspicious transactions involving senior members of the administration of former Ukrainian President Viktor Yanukovych.[7] FIN-2014-A002 was issued on March 6, 2014, apprising financial institutions of recent developments and warning that adverse measures taken against former Ukrainian officials and their close associates will increase the risk that they will seek to move their assets in a deceptive fashion.[8]

Congressional Action

Congress has also taken action, adopting the "Support for Sovereignty, Integrity, Democracy, and Economic Stability of Ukraine Act of 2014" ("Ukraine Act"), which President Obama signed into law on April 3, 2014. The Ukraine Act, among other things, authorizes the President to impose sanctions (asset freezes and visa bans) against persons that the President determines have perpetrated or are responsible for human rights abuses in the Ukraine, or acts intended to undermine the peace, security, stability, sovereignty or territorial integrity of Ukraine. These sanctions largely overlap with those already created under President Obama's Executive Orders.

However, the Ukraine Act also specifically targets corruption by Russian officials, authorizing sanctions against "any official of the Government of the Russian Federation, or a close associate or family member of such an official, that the President determines is responsible for, complicit in, or

Copyright © 2024 Schulte Roth & Zabel LLP

responsible for ordering, controlling or otherwise directing acts of significant corruption" in either Ukraine or Russia. This focus on Russian corruption is not found in the Executive Orders. Since the Act does not itself prohibit dealings with any particular persons, but rather requires President Obama to determine who should be designated, the impact of the Act remains to be seen.

In addition to sanctions, the Ukraine Act directs the U.S. State Department, Department of Justice and Department of Treasury to assist the new Ukrainian Government in recovering assets linked to corruption by former President Yanukovych and other Ukrainian officials.

Implications for Compliance

The sanctions and AML measures described above create compliance risks for companies operating in or otherwise engaged in business dealings involving Russia or Ukraine. According to reports, regulators in Europe and the United States are asking financial institutions for information relating to risks in Russia and Ukraine. For example, the U.S. Securities and Exchange Commission ("SEC") has reportedly contacted investment companies and public funds, including mutual funds, regarding investments in Russia. Likewise, the Bank of England Prudential Regulation Authority has reportedly asked banks to provide details on their exposure to Russia.

U.S. companies should review existing customers, investors, and other counterparties for compliance with Ukraine-related sanctions. If a U.S. company has possession or control of any property interest belonging to an SDN, that property must immediately be blocked, and a Report of Blocked Transactions Form filed with OFAC.

U.S. companies should also ensure that new transactions with customers, investors and other counterparties do not run afoul of the Ukraine-related sanctions. This includes screening proposed investments or transactions involving individuals or entities from Russia or Ukraine against the most up-to-date SDN List.

When performing due diligence — and also when considering whether any existing investments or transactions are subject to blocking — it is important to remember that entities in which an SDN has a 50 percent or greater ownership interest are also considered blocked,[9] and even SDN ownership interests below the 50 percent threshold may warrant careful scrutiny.[10]

Copyright © 2024 Schulte Roth & Zabel LLP
Attorney Advertising

As noted above, OFAC's Ukraine-related sanctions apply only to U.S. persons and not to foreign individuals or entities, including foreign subsidiaries of U.S. parent companies. Nevertheless, it remains impermissible for U.S. persons and U.S. entities, wherever located, to have any dealings with SDNs or to facilitate a non-U.S. person's dealings with SDNs. Additionally, non-U.S. companies must also stay apprised of and comply with applicable sanctions imposed by foreign countries and international organizations.

The application of OFAC sanctions to a particular relationship or transaction often raises complex issues and depends upon an assessment of the specific facts and circumstances involved. Firms should consider reputational as well as legal risk as part of their analysis.

Finally, even when a proposed investment or other transaction involving Russia or Ukraine does not violate OFAC regulations, U.S. companies should be aware of the increased AML risks associated with these regions in light of the Ukraine crisis. As set forth in the FinCEN advisories described above, U.S. financial institutions should be alert to the possibility that former members of the now-deposed Ukrainian regime will seek to transfer potentially illicit funds in a deceptive manner. Likewise, U.S. financial institutions are reminded of the need for enhanced due diligence for transactions involving senior foreign political figures and politically exposed persons ("SFPFs/PEPs"). Transactions even with permitted Russian counterparties, especially those connected to President Putin and the Russian Government, are likely to attract greater scrutiny from U.S. AML prosecutors and regulators.

Authored by Lisa A. Prager, Betty Santangelo, Gary Stein, Peter H. White and Nora Lovell Marchant.

If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

---

[1] The SDN List is subject to constant updates. As of the date of this *Alert*, 32 names appear on the SDN List under the Ukraine programs, including 31 individuals and one bank. *See* OFAC SDN Search, *available at* http://sdnsearch.ofac.treas.gov/.

[2] "Government of the Russian Federation" means the Government of the Russian Federation, any political subdivision, agency or instrumentality thereof, including the Central Bank of the Government of the Russian Federation, and any person owned or controlled by, or acting for or on behalf of, the Government of the Russian Federation.

Copyright © 2024 Schulte Roth & Zabel LLP

[3] OFAC has indicated that government entities are not necessarily blocked even when the leaders of such entities are deemed SDNs. *See* OFAC FAQ 285, *available at* http://www.treasury.gov/resource-center/faqs/Sanctions/Pages/answer.aspx#index ("A government ministry is not blocked solely because the minister heading it is an SDN. U.S. persons should, however, be cautious in dealings with the ministry to ensure that they are not, for example, entering into any contracts that are signed by the SDN.").

[4] *See* OFAC Press Release, *Treasury Sanctions Russian Officials, Members Of The Russian Leadership's Inner Circle, And An Entity For Involvement In The Situation In Ukraine* (March 20, 2014), *available at* http://www.treasury.gov/press-center/press-releases/Pages/jl23331.aspx.

[5] Sanctioned individuals, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2014:066:0026:0030:EN:PDF.

[6] Sanctioned individuals, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2014:078:0016:0021:EN:PDF; http://register.consilium.europa.eu/doc/srv?l=EN&t=PDF&gc=true&sc=false&f=ST%207962%202014%20ADD%201%20REV%202%20DCL%2

[7] *See* FinCEN Advisory, *Guidance to Financial Institutions on Recent Events related to the Departure of Victor Yanukovych and Other Ukrainian Officials* (Feb. 25, 2014), *available at* http://www.fincen.gov/statutes_regs/guidance/html/FIN-2014-A001.html.

[8] *See* FinCEN Advisory, *Updated Guidance to Financial Institutions on Recent Events related to the Departure of Victor Yanukovych and Other Ukrainian Officials* (March 6, 2014), *available at* http://www.fincen.gov/statutes_regs/guidance/html/FIN-2014-A002.html.

[9] *See* OFAC FAQ 10, *available at* http://www.treasury.gov/resource-center/faqs/Sanctions/Pages/answer.aspx#index ("Entities that a person on the SDN List owns (defined as a direct or indirect ownership interest of 50 percent or more) are also blocked, regardless of whether that entity is separately named on the SDN List.").

[10] *See* OFAC Guidance on Entities Owned by Persons Whose Property and Interests in Property are Blocked, *available at* http://www.treasury.gov/resource-center/sanctions/Documents/licensing_guidance.pdf ("U.S. persons are advised to act with caution when considering a transaction with a non-

Copyright © 2024 Schulte Roth & Zabel LLP
Attorney Advertising

blocked entity in which a blocked person has a significant ownership interest that is less than 50 percent or which a blocked person may control by means other than a majority ownership interest. Such entities may be the subject of future designation or enforcement action by OFAC.”).

This information has been prepared by Schulte Roth & Zabel LLP (“SRZ”) for general informational purposes only. It does not constitute legal advice, and is presented without any representation or warranty as to its accuracy, completeness or timeliness. Transmission or receipt of this information does not create an attorney-client relationship with SRZ. Electronic mail or other communications with SRZ cannot be guaranteed to be confidential and will not (without SRZ agreement) create an attorney-client relationship with SRZ. Parties seeking advice should consult with legal counsel familiar with their particular circumstances. The contents of these materials may constitute attorney advertising under the regulations of various jurisdictions.

Related People

Betty Santangelo

New York

Peter White

Of Counsel

Washington, DC

Practices

BANK REGULATORY

Copyright © 2024 Schulte Roth & Zabel LLP

INSURANCE

LITIGATION

SEC ENFORCEMENT AND WHITE COLLAR DEFENSE

Attachments

Download Alert

Copyright © 2024 Schulte Roth & Zabel LLP

Attorney Advertising