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US AND ALLIES ANNOUNCE SANCTIONS ON RUSSIA AND SEPARATIST REGIONS OF UKRAINE

To Our Clients and Friends:

On February 21 and 22, 2022, the United States, the European Union, the United Kingdom, Australia, and Japan issued and/or announced sanctions targeting Russia and the Russia-backed separatist regions of Ukraine known as the Donetsk People's Republic ("DNR") and the Luhansk People's Republic ("LNR"). The United States took the first step by issuing broad jurisdiction-based sanctions on the two regions, similar to the existing sanctions on the Crimea region of Ukraine, and followed up with additional sanctions targeting Russia's financial system. NATO allies also announced sanctions—including targeted designations by the United Kingdom and a sanctions package by the European Union—and non-NATO allies promised tough sanctions in close coordination. These actions are only among a few of several tools we expect the United States and its allies will use in the coming days and weeks as Russia continues to stoke military tension in the region.

These actions follow nearly a decade of lasting conflict in eastern Ukraine and a quick escalation over the past few weeks. After the 2014 Ukrainian revolution and the Euromaidan movement, which saw a pro-Western government elected in Ukraine, pro-Russia protests against the new government began in eastern Ukraine. These protests in the DNR and LNR regions eventually developed into full-scale fighting, with Russia backing the separatists against the Ukrainian military and more than 10,000 people killed in the conflict. Shaky ceasefires between the two sides have existed for several years, but in recent days, artillery shelling has increased along with other violations of the ceasefire agreements, with the Ukrainian government claiming that these attacks were orchestrated by Russia or pro-Russia separatists in the region.

In response to formal appeals from the *de facto* leaders of the breakaway regions for sovereign recognition from Russia, Russian president Vladimir Putin convened a meeting of his security council on Monday, February 21, 2022 under the pretext of seeking recommendations on how to answer the requests. After the meeting of the council, Putin delivered a televised address to the public, referring to eastern Ukraine as "historically Russian territory" and saying that it is "necessary to take a long overdue decision to immediately recognize the independence and sovereignty of the Donetsk People's Republic and the Luhansk People's Republic." Immediately thereafter, Putin ordered Russian troops to enter the regions for a "peacekeeping" mission under the treaties of "friendship and mutual assistance" that Russia ratified that same day with the individual regions. All diplomatic efforts to maintain the territorial integrity of Ukraine while the parties sought to ease building tensions thus suffered a serious setback.

US Issues New Executive Order Imposing Sweeping Sanctions on Separatist Regions

Just hours after Putin's televised speech, President Biden signed a new Executive Order issuing broad sanctions on the DNR and LNR regions of Ukraine, and any other regions of Ukraine as may be determined by the Secretary of the Treasury, in consultation with the Secretary of State (collectively, the "Covered Regions"). The Executive Order is nearly identical to Executive Order 13685 that announced comprehensive sanctions on the Crimea region of Ukraine in 2014.

First, the Executive Order prohibits: (1) new investment in the Covered Regions by a U.S. person; (2) import of any goods, services, or technology from these regions to the United States; and (3) export of any goods, services, or technologies from the United States or by a U.S. person to these regions. The Executive Order further prohibits U.S. persons from financing, facilitating, or guaranteeing transactions by foreign persons that U.S. persons would be prohibited from engaging directly.

Second, the Executive Order authorizes blocking sanctions on any person determined by the Secretary of the Treasury, in consultation with the Secretary of State, to be: (1) a person operating in the Covered Regions; or (2) a leader, official, senior executive officer, or board member of an entity operating in the Covered Regions. The Executive Order also authorizes sanctions on an entity determined to be owned or controlled by a blocked person pursuant to the Executive Order, or any person who has provided material support for a blocked person pursuant to the Executive Order. No such individual designations have yet been made, which is very similar to how OFAC responded at the inception of Executive Order 13685.

Concurrent with the signing of the Executive Order, OFAC issued six general licenses:

- General License 17, "Authorizing the Wind Down of Transactions Involving the So-called Donetsk People's Republic or Luhansk People's Republic Regions of Ukraine" authorizes all prohibited transactions "that are ordinarily incident and necessary to the wind down of transactions involving" the Covered Regions <u>until March 23, 2022</u>.

- General License 18, "Authorizing the Exportation or Reexportation of Agricultural Commodities, Medicine, Medical Devices, Replacement Parts and Components, or Software Updates to Certain Regions of Ukraine and Transactions Related to the Coronavirus Disease 2019 (COVID-19) Pandemic" authorizes the export of agricultural commodities, medicine, medical devices, replacement parts and components, or software updates to the Covered Regions. This authorization is similar to that of the existing General License 4 with respect to the Crimea region, but is more expansive in that it does not include the exclusions that are in General License 4 (e.g., export to military or law enforcement purchasers, certain agricultural commodities, and certain medicines), that it expands the scope to software updates in addition to replacement parts, and that it includes a separate COVID-19 authorization.

- General License 19, "Authorizing Transactions Related to Telecommunications and Mail" authorizes transactions that are ordinarily incident and necessary to the receipt or transmission of telecommunications in the Covered Regions. This authorization is similar to the existing General License 8 with respect to the Crimea region.

- General License 20, "Official Business of Certain International Organizations and Entities" authorizes official business of certain international organizations and entities in the Covered Regions. Of note, the list of international organizations includes the Organization for Security and Co-operation in Europe, an entity that has been actively seeking to de-escalate the conflict in recent days.

- General License 21, "Authorizing Noncommercial, Personal Remittances and the Operation of Accounts" authorizes transactions that are ordinarily incident and necessary to the transfer of noncommercial, personal remittances to or from the Covered Regions. This authorization is similar to the existing General License 6 with respect to the Crimea region.

- General License 22, "Authorizing the Exportation of Certain Services and Software Incident to Internet-Based Communications" authorizes export of certain services incident to the exchange of personal communications over the internet or software necessary to enable such services in the Covered Regions. This is similar to the existing General License 9 with respect to the Crimea region, but is more expansive in that it does not require the services and software to be widely available to the public with no cost to the user.

The issuance of these expansive general licenses is in line with the White House's repeated messaging that the sanctions "are not directed at the people of Ukraine" or "the innocent people who live in the so-called DNR and LNR regions." Particularly during the COVID-19 pandemic, the Biden administration has continued to include broad humanitarian exceptions in new sanctions measures, including those taken in response to the situations in Myanmar and Ethiopia. It is noteworthy that OFAC further created an expansive COVID-19 authorization for transactions related to the prevention, diagnosis, or treatment of the COVID-19 pandemic, without any specific definition or exception.

General License 17 is also consistent with OFAC's past practices of allowing parties a period of time to adjust to significant new sanctions measures to minimize the immediate disruption to the global economy. Similar to the more recent wind-down licenses from OFAC, there is no requirement for U.S. persons participating in authorized transactions to file a report with OFAC, which reduces the administrative burden of relying on the license. However, the 30-day wind-down period is much shorter than the typical 60- to 90-day periods that OFAC has granted in announcing other sanctions measures. It is likely that future wind-down licenses from OFAC regarding sanctions targeting Russia will be similarly brief.

Parties planning to rely on these general licenses should note that all six general licenses expressly limit their authorizations to transactions and activities that are prohibited by this particular Executive Order. The general licenses do not authorize transactions with persons or entities designated pursuant to other sanctions programs. As a result, parties should be careful not to engage in transactions and activities that are prohibited under another authority, such as the sectoral sanctions under Executive Order 13662. Parties should also take note of the differences between the general licenses granted with respect to the Crimea sanctions and to the DNR and LNR sanctions, in case a counterparty is sanctioned under both Executive Order 13685 and the new Executive Order.

US Imposes Sanctions on Russian Financial Services Sector

On February 22, 2022, OFAC designated to the SDN List two financial institutions that it determined are crucial to financing the Russian defense industry—Corporation Bank for Development and Foreign

Economic Affairs Vnesheconombank (VEB) and Promsvyazbank Public Joint Stock Company (PSB)—along with 42 of their subsidiaries. OFAC also designated three individuals—Denis Aleksandrovich Bortnikov, Petr Mikhailovich Fradkov, and Vladimir Sergeevich Kiriyenko—who OFAC determined were "powerful Russians in Putin's inner circle."

All of the designations were made under the authority of the Executive Order 14024, which we discussed in depth in a previous update. Importantly, Executive Order 14024 had authorized blocking sanctions against persons determined to operate in certain sectors of the Russian economy, with specific sectors to be determined by the Secretary of the Treasury, in consultation with the Secretary of State. When Executive Order 14024 was issued in April 2021, OFAC had identified the technology sectors and defense and related materiel sector as potential targets of future designations. In the most recent action taken on February 22, 2022, OFAC additionally identified the financial services sector of the Russian economy, making it easier for the United States to use a single, consolidated sanctions tool to target the entire financial services sector. OFAC accompanied this determination with FAQ 964, noting that its determination merely lays the groundwork for future sanctions against persons that operate in the financial services sector, rather than actually serving as sanctions on the entire financial services sector.

Additionally, OFAC issued Directive 1A, amending and superseding Directive 1 that was issued under Executive 14024. Importantly, Directive 1A includes restrictions on the participation in the secondary market for ruble or non-ruble denominated bonds issued after March 1, 2022 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. As a result of this new Directive 1A, the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, and the Ministry of Finance of the Russian Federation have been designated to the Non-SDN Menu-Based Sanctions List.

Concurrent with these additional sanctions, OFAC issued two general licenses:

- General License 2, "Authorizing Certain Servicing Transactions Involving State Corporation Bank for Development and Foreign Economic Affairs Vnesheconombank" authorizes all prohibited transactions "that are ordinarily incident and necessary to the servicing of bonds issued <u>before March 1, 2022</u> 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," but to the extent that such transaction is not prohibited by the new Directive 1A.

- General License 3, "Authorizing the Wind Down of Transactions Involving State Corporation Bank for Development and Foreign Economic Affairs Vnesheconombank" authorizes all prohibited transactions "that are ordinarily incident and necessary to the wind down of transactions involving" VEB for a 30-day period <u>until March 24, 2022</u>.

Again, parties planning to rely on these general licenses should note that the general licenses expressly limit their authorizations to transactions and activities that are prohibited by Executive Order 14024.

EU Announces Sanctions Package to be Implemented

The EU has announced, yet not formally issued, new sanctions on Russia. While in the morning of February 22, 2022, the presidents of the European Council and the European Commission had welcomed "the steadfast unity of [EU] Member States and their determination to react with robustness and speed," the subsequent announcement of the specific contemplated measures was more limited in scope than expected by many and only came after a surprisingly lengthy meeting of EU Foreign Affairs Ministers. The formal issuance and implementation of the contemplated measures is now expected in the course of the week.

First, in what the EU has now referred to as "solid package" of "calibrated measures," EU financial sanctions (broadly comparable to U.S. SDN designations) will target individuals and entities involved in the violations of international law by the Kremlin, including in the recognition of the Donetsk and Luhansk regions as independent entities.

Second, the EU will target banks that finance the Russian military apparatus and contribute to the destabilization of Ukraine. Such banks have not yet been named and will either be targeted via EU financial sanctions or via more limited EU economic sanctions (broadly comparable to U.S. SSI designations).

Third, the EU has announced that it plans to ban trade between the EU and the Donetsk and Luhansk regions by implementing comprehensive EU Economic Sanctions comparable to those implemented after the annexation by Russia of Crimea in 2014.

Finally, the EU announced new measures to restrain Russian efforts to raise further capital on EU's financial markets by limiting respective access for the Russian state and government. Such measures will likely take the form of targeted EU Economic Sanctions and prohibit or at least limit dealings with, for example, transferable securities and money-market instruments with a certain maturity and prohibit making loans or credit to those targeted.

The EU also announced that it had prepared and stands ready to adopt additional measures at a later stage if needed in the light of further developments.

Germany Stops Certification of Nord Stream 2

As a first reaction, the German Chancellor Olaf Scholz announced that the certification of the Nord Stream 2 pipeline has been stopped, and thus the pipeline will not become operational until further notice. This action was perhaps the least expected response and carries significant practical impact. The Nord Stream 2 project was intended to supply energy from Russia to the European Union, and Germany—along with other EU member states—had so far contested any attempts to impose sanctions on the Nord Stream 2 project in light of Russian aggression, in part due to the European Union's heavy reliance on energy sources from Russia. With this action, Germany sent a clear message that it stands ready to join severe sanctions against Russia.

United Kingdom Sanctions Russian Banks and Oligarchs

On February 10, 2022, the UK pre-emptively amended its legislation on Russia sanctions—the Russia (Sanctions) (EU Exit) Regulations 2019 (S.I. 2019/855) (the "UK Russia Sanctions Regulations")—via the enactment of The Russia (Sanctions) (EU Exit) (Amendment) Regulations 2022 (SI 2022/123) (the "Amended Regulations").

The Amended Regulations widened the scope of the UK Russia Sanctions Regulations by expanding its designation criteria. The designation criteria now include entities and individuals that are involved in "obtaining a benefit from or supporting the Government of Russia." Previously, the UK could only impose travels bans or asset freezes on those involved in "destabilising Ukraine or undermining or threatening the territorial integrity, sovereignty or independence of Ukraine."

For the purposes of the Amended Regulations, being "involved in obtaining a benefit from or supporting the Government of Russia" includes, among other things, carrying on business "of economic significance" or "in a sector of strategic significance" to the Government of Russia, those sectors being the Russian chemicals, construction, defense, electronics, energy, extractives, financial services, information, communications, digital technologies, and transport sectors. This is therefore a very significant expansion in the scope of the designation criteria which empowers the UK to impose sanctions on a wide range of businesses that may not necessarily have a strong nexus to the Russian government, save that the nature of their business and/or the sector(s) in which they operate are of economic significance to the Russian government.

Using its new powers under the Amended Regulations, the UK government updated the UK Sanctions List on February 22, 2022 by designating five Russian banks (Bank Rossiya, Black Sea Bank for Development and Reconstruction, Joint Stock Company Genbank, IS Bank, Public Joint Stock Company Promsvyazbank) as well as three wealthy individuals (Gennadiy Nikolayevich Timchenko, Boris Romanovich Rotenberg and Igor Arkadyevich Rotenberg) as being subject to an asset freeze.

The UK's Prime Minister, Boris Johnson, has described this sanctions package as "the first tranche, the first barrage" of what the UK is prepared to do. Foreign Secretary, Liz Truss, said in her statement that "this first wave of sanctions will hit oligarchs and banks close to the Kremlin. It sends a clear message that the UK will use [its] economic heft to inflict pain on Russia and degrade their strategic interests." She further stated that "in the event of further aggressive acts by Russia against Ukraine," the UK has prepared "an unprecedented package of further sanctions ready to go. These include a wide-ranging set of measures targeting the Russian financial sector, and trade." However, for some in the UK, these measures do not go far enough, and Boris Johnson is under pressure to impose tougher sanctions.

Allies Outside NATO Join in Announcing Tough Response

Japan's Minister of Foreign Affairs Hayashi Yoshimasa stated that Japan would continue to monitor the development of the situation in Ukraine with serious concern and coordinate a tough response, including sanctions in cooperation with the international community.

Australia's Minister of Foreign Affairs declared that the Australian Government was coordinating closely with the United States, United Kingdom, European Union, and other governments around the world to ensure there were severe costs for Russia's aggression and that, along with its partners, Australia was prepared to announce swift and severe sanctions that would target key Russian individuals and entities responsible for undermining Ukraine's sovereignty and territorial integrity.

Possible Next Steps

There has been much speculation in recent days about the sanctions packages that would be revealed upon Russia's invasion of Ukraine. So far, many world leaders have stopped short of calling Russia's recognition of the two regions and his deployment of the Russian military to these regions a full-scale invasion, perhaps in part as an effort to deescalate tension or to leave space for additional sanctions if the situation worsens. However, the recent measures allow more authority for the Western countries to issue additional sanctions in case of further escalation—such as a new Executive Order that authorizes sanctions on persons operating in the separatist regions of Ukraine and a financial services sector determination that authorizes sanctions on persons operating in the Russian financial services sector. As tensions continue to rise, we will likely see more series of tools from the NATO countries and their allies to exert economic pressure on Russia to deescalate the ongoing crisis in Ukraine and withdraw its army from Ukraine's borders. Companies should continue to pay attention to the ongoing developments and proactively assess their exposure to the sanctions and export controls measures being discussed.

In the lead up to the recent sanctions, leaders of the NATO countries engaged in close coordination and dialogue and had reported that they have "wrapped up" and are "unified" on potential sanctions packages to be used. However, we have seen varying degrees of severity and speed in the measures that each of the governments were able to impose immediately following the action from Russia. We expect there to be continued effort for coordination and convergence across the various jurisdictions, but we are closely tracking the differences in the sanctions imposed in different jurisdictions and the resulting compliance impact for companies operating in the global market.

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