

Impact of Recent U.S. Secondary Sanctions Authority Targeting Foreign Financial Institutions Supporting Russia's Military-Industrial Base

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As the second anniversary of the conflict in Ukraine approaches, the United States, the European Union, and the United Kingdom continue to focus on and tighten sanctions against Russia, with a particular emphasis on preventing circumvention and evasion of sanctions. For example, 2023 ended with several significant regulatory developments, including the EU 12th package of sanctions against Russia, discussed in our earlier [alert](#), and new U.S. sanctions-related authority targeting foreign financial institutions (“FFIs”) supporting Russia’s military-industrial base. This update focuses on the latter development, which is a significant development for FFIs that remain engaged in business involving Russia, even if such business is undertaken outside of U.S. jurisdiction.

Increased Threat of Secondary Sanctions for Foreign Financial Institutions

Late last year, President Biden issued Executive Order (“E.O.”) 14114¹ authorizing the imposition of secondary sanctions (which can be

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¹ Executive Order 14114, “Taking Additional Steps with Respect to the Russian Federation’s Harmful Activities”, 88 Fed. Reg. 89271 (Dec. 22, 2023), <https://www.govinfo.gov/content/pkg/FR-2023-12-26/pdf/2023-28662.pdf>.
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imposed on non-U.S. persons for engaging in targeted activities undertaken outside of U.S. jurisdiction) on FFIs² determined by the U.S. government to have conducted or facilitated any “significant” transaction or transactions:

- for or on behalf of parties sanctioned under E.O. 14114 for operating or having operated in the technology, defense and related materiel, construction, aerospace, or manufacturing sectors of the Russian economy (or other such sectors as may be determined by the U.S. government to support Russia’s military-industrial base);³
- or provided any service involving Russia’s military-industrial base, including the sale, supply or transfer, directly or indirectly, to Russia of any critical item or class of items as may be determined by the U.S. government.⁴

The targeted transactions and services may include maintaining accounts, transferring funds, or providing other financial services (*i.e.*, payment processing, trade finance, insurance) for any persons designated for

operating in the specified sectors or for any persons, either inside or outside Russia, that support Russia’s military-industrial base.⁵ The list of critical items⁶ that support Russia’s military-industrial base includes certain machine tools and manufacturing equipment, manufacturing materials for semiconductors and related electronics, electronic test equipment, propellants, chemical precursors for propellants and explosives, lubricants and lubricant additives, bearings, advanced optical systems, and navigation instruments. Knowledge of the FFIs or lack of reasonable due diligence is not a prerequisite for the imposition of sanctions under E.O. 14114, which significantly increases the sanctions risk for FFIs engaging in Russia-related activities or operations, even when such activities do not involve a violation of U.S. law or a U.S. jurisdictional nexus.

E.O. 14114 was accompanied by White House statements noting that FFIs “risk losing access to the U.S. financial system if they facilitate significant transactions relating to Russia’s military-industrial base.”⁷ In addition to these statements, and perhaps in

² Under Executive Order 14114, “foreign financial institution” is any foreign entity that is engaged in the business of accepting deposits; making, granting, transferring, holding, or brokering loans or credits; purchasing or selling foreign exchange, securities, futures or options; or procuring purchasers and sellers thereof, as principal or agent. It includes depository institutions; banks; savings banks; money services businesses; operators of credit card systems; trust companies; insurance companies; securities brokers and dealers; futures and options brokers and dealers; forward contract and foreign exchange merchants; securities and commodities exchanges; clearing corporations; investment companies; employee benefit plans; dealers in precious metals, stones, or jewels; and holding companies, affiliates, or subsidiaries of any of the foregoing. “Foreign financial institution” does not include the international financial institutions identified in 22 U.S.C. 262r(c)(2), the International Fund for Agricultural Development, the North American Development Bank, or any other international financial institution so notified by the Office of Foreign Assets Control. For additional guidance on the definition of “foreign financial institution,” “Russia’s military industrial base,” and “significant transaction,” *see* OFAC’s FAQ 1151 (Dec. 22, 2023), available at <https://ofac.treasury.gov/faqs/1151>.

³ Russian military-industrial base is defined in OFAC’s Determination of December 22, 2023 pursuant to Section 11(a)(ii) of Executive Order 14024, available at: <https://ofac.treasury.gov/media/932446/download?inline>.

⁴ Executive Order 14114 specifically amends Executive Order 14024 to increase the secondary sanctions risk for foreign financial institutions. Executive Order 14024 is available at

<https://ofac.treasury.gov/media/57936/download?inline>. Executive Order 14114 also amends Executive Order 14068, which expanded the Russian seafood import ban to include products whether or not “incorporated or substantially transformed into another product” outside of Russia. *See also* OFAC, Determination of December 22, 2023 pursuant to Section 1(a)(i)(B) of Executive Order 14068, available at

<https://ofac.treasury.gov/media/932451/download?inline>.

⁵ OFAC, “Guidance for Foreign Financial Institutions on OFAC Sanctions Authorities Targeting Support to Russia’s Military Industrial Base” (Dec. 22, 2023), available at

<https://ofac.treasury.gov/media/932436/download?inline>.

⁶ OFAC, Determination of December 22, 2023 pursuant to Section 11(a)(ii) of Executive Order 14024, available at:

<https://ofac.treasury.gov/media/932446/download?inline>.

⁷ White House, “FACT SHEET: Biden Administration Expands U.S. Sanctions Authorities to Target Financial Facilitators of Russia’s War Machine” (Dec. 22, 2023), available at <https://www.whitehouse.gov/briefing-room/statements-releases/2023/12/22/fact-sheet-biden-administration-expands-u-s-sanctions-authorities-to-target-financial-facilitators-of-russias-war-machine/>; *see also* White House, “Statement from National Security Advisor Jake Sullivan on Expanding Sanctions Authorities Against Russia’s Military Industrial Base” (Dec. 22, 2023), available at <https://www.whitehouse.gov/briefing-room/statements-releases/2023/12/22/statement-from-national-security-advisor-jake-sullivan-on-expanding-sanctions-authorities-against-russias-military-industrial-base/>.

recognition of the difficulty that FFIs may have in confirming whether customers are involved in the supply of specified items or Russia's military-industrial base, the U.S. Department of the Treasury, Office of Foreign Assets Control ("OFAC") released a compliance advisory⁸ providing guidance to FFIs regarding how to identify sanctions risks and implement controls following issuance of E.O. 14114.⁹ For example, OFAC provided examples of controls that FFIs should implement commensurate with their risk and current exposure to Russia's military-industrial base and its supporters, including (1) reviewing customer bases to determine exposure to customers involved in the specified sectors or who conduct business with designated persons in the specified sectors and customers that may be involved in the sale, supply, or transfer of specified items to Russia or to jurisdictions previously identified as posing a high risk of Russian sanctions evasion;¹⁰ (2) communicating compliance expectations to customers, including informing them that they may not use their accounts to do business with designated persons operating in the specified sectors or conduct any activity involving Russia's military-industrial base; (3) sending questionnaires to customers known to deal in or export specified items to better understand their counterparties; and (4) obtaining attestations from customers that they do not operate in the specified sectors, engage in any sales or transfers of the specified items to Russia, or otherwise conduct any

transactions involving Russia's military-industrial base. The guidance makes clear that these steps are in addition to baseline customer due diligence procedures.

With respect to FFIs determined to engage in activities covered by E.O. 14114, the U.S. government is authorized to (1) prohibit the opening of, or prohibit or impose strict conditions on the maintenance of, correspondent accounts or payable-through accounts in the United States for such FFIs, or (2) impose blocking sanctions on such FFIs (*i.e.*, designation of such FFIs on the list of Specially Designated Nationals and Blocked Persons ("SDNs") maintained by OFAC).

In addition to the above-referenced potential secondary sanctions under E.O. 14114, U.S. secondary sanctions can be imposed on non-U.S. persons that undertake a number of activities relating to Russia, including knowingly engaging in significant transactions with parties subject to U.S. sanctions against Russia, providing material assistance or support to SDNs, or operating in certain sectors of the Russian economy, including: technology;¹¹ defense and related materiel;¹² financial services;¹³ aerospace; electronics; marine;¹⁴ accounting; trust, and corporate formation services; management consulting;¹⁵ quantum computing;¹⁶

⁸ OFAC, "Guidance for Foreign Financial Institutions on OFAC Sanctions Authorities Targeting Support to Russia's Military Industrial Base" (Dec. 22, 2023), available at <https://ofac.treasury.gov/media/932436/download?inline>.

⁹ For additional guidance, please see OFAC's FAQ's 1146-1157, available at [https://ofac.treasury.gov/faqs/search?field_faq_number\[min\]=1146&field_faq_number\[max\]=1157](https://ofac.treasury.gov/faqs/search?field_faq_number[min]=1146&field_faq_number[max]=1157).

¹⁰ Jurisdictions that have been previously identified as posing a high risk of Russian sanctions evasion include Belarus, China, Turkey, Armenia, and Uzbekistan. See "Department of Commerce, Department of Treasury, and Department of Justice Tri-Seal Compliance Note: Cracking Down on Third-Party Intermediaries Used to Evade Russia-Related Sanctions and Export Controls" (Mar. 22, 2023), available at <https://www.justice.gov/file/1571551/download>.

¹¹ Executive Order No. 14024, "Blocking Property With Respect To Specified Harmful Foreign Activities of the Government of the

Russian Federation," 86 Fed. Reg. 20249 (Apr. 15, 2021), available at

<https://ofac.treasury.gov/media/57936/download?inline>.

¹² Executive Order 14024, Section 1(a)(i), available at <https://ofac.treasury.gov/media/57936/download?inline>.

¹³ OFAC, Determination of February 22, 2022 pursuant to Executive Order No. 14024, available at

<https://ofac.treasury.gov/media/918726/download?inline>.

¹⁴ OFAC, Determination of March 31, 2022 pursuant to Executive Order No. 14024, available at

<https://ofac.treasury.gov/media/921226/download?inline>.

¹⁵ OFAC, Determination of May 8, 2022 pursuant to Section 1(a)(i) of Executive Order 14024, available at

<https://ofac.treasury.gov/media/922951/download?inline>.

¹⁶ OFAC, Determination of September 15, 2022 pursuant to Section 1(a)(i) of Executive Order 14024, available at

<https://ofac.treasury.gov/media/926586/download?inline>.

metals and mining;¹⁷ architecture; engineering; construction; manufacturing; and transportation.¹⁸

Although secondary sanctions in practice involve considerable discretion and political calculation, the increased threat of secondary sanctions has the practical effect of deterring FFIs from engaging in potentially high-risk or sanctionable conduct and encouraging them to implement heightened diligence procedures. Indeed, it has been reported that since E.O. 14114 was issued, banks in Turkey, China, the UAE, and Central Asia have been delaying or refusing to process Russia-related payments.¹⁹

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¹⁷ OFAC, Determination of February 24, 2023 pursuant to Section 1(a)(i) of Executive Order 14024, available at <https://ofac.treasury.gov/media/931336/download?inline>.

¹⁸ OFAC, Determination of May 19, 2023 pursuant to Section 1(a)(i) of Executive Order 14024, available at <https://ofac.treasury.gov/media/931771/download?inline>.

¹⁹ See e.g. Regulation Asia, “US Sanctions Prompt Turkish Banks to Reject Russian Payments” (Jan. 22, 2024), available at:

<https://www.regulationasia.com/us-sanctions-prompt-turkish-banks-to-reject-russian-payments/>; The Moscow Times, “Major Chinese Banks Halts All Settlements with Russia – Vedomosti” (Feb. 7, 2024), available at <https://www.themoscowtimes.com/2024/02/07/major-chinese-bank-halts-all-settlements-with-russia-vedomosti-a84001>.