What’s the Impact of Russian Sanctions on Your Organization?

regulatory BSA-AML OFAC

Summary: The broad, complex sanctions imposed on Russia following its second invasion of Ukraine have been very challenging for financial institutions. CFIs may have to choose between managing the sanctions’ complications or simply avoiding relationships that would require navigating them.

Approximately 50 Fabergé eggs were commissioned by the Russian Imperial family in the late 19th and early 20th centuries. But it isn’t just their rarity that makes these bejeweled eggs remarkable — it’s the intricacy of the designs and the materials used that contribute to their value. The eggs are known for their unique craftsmanship — one even resembles a bay tree, covered by 325 individual nephrite leaves and hundreds of diamonds, pearls, and rubies. These eggs took a lot of time and attention to detail to produce, but the end result is museum-worthy.

Similarly complex in execution, relationships with Russian clients may require quite a lot of due diligence work, in light of the sanctions that the US and other countries have enacted against Russia. Imagine that your community financial institution (CFI) is approached by a potential new business client. The owner is a Russian citizen and permanent, legal US resident. She runs a retail jewelry store. Can you have her as a customer?

Now imagine that the same woman, still a Russian citizen and still here legally, runs a jewelry store in the US. But she owns that store as part of a group of owners, and the group’s other members are back home in Russia. Is this a customer your CFI should do business with?

The Moving Target of Russian Sanctions

Since the first sanctions began in 2022, the answers to these questions have gotten increasingly complicated. Early last year, the U.S. Treasury Department announced “unprecedented and expansive sanctions against Russia” designed to impose “swift and severe economic costs” to the country’s decision to invade Ukraine. The US and EU have since added more sanctions against individuals, organizations, and sectors in countries enabling Russian aggression against Ukraine — a list that includes Belarus and Iran.

“The last year has been all about Russia,” says Will Schisa, an attorney at Davis Polk and a former attorney at the Office of Foreign Assets Control’s (OFAC) legal office. “It’s really been an unprecedented sanctions effort in terms of its scale applied to a major world economy.”

Sanctions and Punishments for Breaking Them

The sanctions forbid US individuals and entities — which certainly includes financial institutions — from doing business with individuals and companies on the Specially Designated Nationals (SDN) list. Anyone or anything on the Consolidated Sanctions List (CSL), which covers restricted parties that aren’t on the SDN list, is also out. The OFAC also has restriction lists, such as the Sectoral Sanctions Identification (SSI) list, the Non-SDN Iranian Sanctions Act (NS-ISA), and the Foreign Sanctions Evaders List (FSE).

Companies that deal with foreign individuals and companies have a duty to know the end-to-end provenance of all the goods, services, and participants in a transaction chain. They are responsible for avoiding any deals with sanctions implications.

OFAC administers these rules and has the power to grant exceptions. Offenders can face fines of between a few thousand and several million dollars, as well as up to 30Ys in prison.

Keeping Track of Sanctions and Who They Affect

In principle, any CFI is free to do business with any entity that isn’t on one of the lists of prohibited actors. But to do that, you need to keep track of those lists, a job that typically requires software to be updated consistently, if not in real time. You’ll also need to navigate exceptions to US sanctions.

You’ll also require an understanding of how US sanctions may intersect with sanctions issued by the European Union and United Kingdom, which are similar but not identical to US sanctions. A deal that involves businesses in multiple countries might be sanctioned by one country but not by the others. That could make it legal in the US but also impractical, as any deal is likely to falter.

Even with a business that involves just two countries, you will need to assess their overall sanctions risk and boost your due diligence around transactions and customers that expose you to Russian individuals and companies. Also, remember that, as part of overall sanctions, Russia’s largest banks are no longer permitted to participate in the SWIFT network. That can make moving money to and from Russia much more difficult.

Can you take on the business from our first example as a client? Probably. As long as the woman who owns the jewelry shop isn’t on a list of sanctioned entities, you’re in the clear. Bear in mind, though, that she may find it difficult to import jewelry from Russia, if that’s part of her business.

What about the second example, where some of the jewelry store owners are Russians who live in Russia? Again, as long as the store and its owners aren’t on a list of sanctioned entities, you can write them a loan. To ensure this, however, you’ll need to do quite a bit of due diligence on the Russian owners, and you’ll still have the problem of sending money to or receiving money from Russia. Depending on how much you value the potential client, you might decide that the work involved isn’t worth the hassle.

YOUR INTERNATIONAL PLATFORM OR OURS? YOU CHOOSE!

ECONOMY & RATES

Rates As Of: 05/22/2023 05:33AM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	5.29	0.19	0.87
6M	5.36	0.30	0.60
1Y	5.02	0.28	0.31
2Y	4.26	0.25	-0.17
5Y	3.74	0.26	-0.26
10Y	3.69	0.26	-0.19

30Y	3.95	0.27	-0.02

FF Market	**FF Disc**	**IORB**
5.08	5.25	5.15
SOFR	**Prime**	**OBFR**
5.05	8.25	5.07