

INTERNATIONAL FINANCE - SPRING 2022

SANCTIONS 2

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After the Russian annexation of Crimea in 2014 the EU and the US imposed sanctions on Russia.² Recent sanctions relating to the invasion of Ukraine beginning on February 24, 2022 therefore build on an earlier sanctions regime which, clearly, was not effective in dissuading Russia's aggression with respect to Ukraine. The 2022 sanctions measures are extensive and complex to track,³ and are having and will continue to have a significant impact on Russia and the rest of the world.⁴ Commentators have been expecting Russia and Russian state entities to default on foreign-currency denominated debt, although Russia did make an interest payment of \$117m on March 16 to avoid a

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² See, e.g., EO 13660 Blocking Property of Certain Persons Contributing to the Situation in Ukraine, 79 Fed. Reg. 13493 (Mar. 10, 2014); EO 13661 Blocking Property of Additional Persons Contributing to the Situation in Ukraine, 79 Fed. Reg. 15535 (Mar. 19, 2014); EO 13662 Blocking Property of Additional Persons Contributing to the Situation in Ukraine, 79 Fed. Reg. 16169 (Mar. 24, 2014); EO 13685 Blocking Property of Certain Persons and Prohibiting Certain Transactions with Respect to the Crimea Region of Ukraine 79 Fed. Reg. 77357 (Dec. 24, 2014).

³ See, e.g., <https://graphics.reuters.com/UKRAINE-CRISIS/SANCTIONS/byvrrjenzmve/>; <https://complyadvantage.com/insights/sanctions-on-russia-compliance-updates/>. See also, Norman Eisen, Aaron Klein, Mario Picon, Robin J. Lewis, Lilly Blumenthal, Scott Johnston & Charlie Loudon, The Brookings Sanctions Tracker (Mar. 14, 2022) at <https://www.brookings.edu/research/the-brookings-sanctions-tracker/>.

⁴ See, e.g., Pablo Hernández de Cos, Governor of the Bank of Spain, the Economic Setting Following the Invasion of Ukraine and the Economic Policy Response, Speech (Mar. 15, 2022) ("The Russian invasion of Ukraine, on 24 February, and the western world's response, which has led to the imposition of unprecedented economic sanctions on Moscow, represent a new and foreseeably hugely significant shock, with adverse consequences in terms of a weaker economic performance and greater inflationary pressures."); Joint Statement of Heads of International Financial Institutions with Programs in Ukraine and Neighboring Countries (Mar.17, 2022) ("The entire global economy will feel the effects of the crisis through slower growth, trade disruptions, and steeper inflation, harming especially the poorest and most vulnerable. Higher prices for commodities like food and energy will push inflation up further. Countries, particularly those neighboring Ukraine will suffer disruptions in trade, supply chains and remittances as well as surges in refugee flows. Reduced confidence and higher investor uncertainty will impact asset prices, tighten financial conditions, and could even generate capital outflows from emerging markets.")

default.⁵ Ukraine has also suffered significant financial harms,⁶ as well as devastation to its people.

Unusually, because of the exceptional circumstances, press coverage of the sanctions is extensive. Preparation for the sanctions response began as the Russian troop build-up was observed towards the end of 2021, including attempts by the US to co-ordinate with other countries.⁷ And since implementation of sanctions measures have begun we have seen some businesses responding to Russia's actions by closing down their business activities in and with Russia even where those activities were not prohibited by sanctions measures.⁸

In this section of the materials I want to focus on some aspects of the US Russia/Ukraine sanctions regime, particularly from the perspective of those who are charged with complying with sanctions. I am not going to focus here on sanctions measures directed at individuals, although this is a significant component of the regime. In the first set of sanctions materials I addressed some issues relating to sanctions measures directed at individuals. But let's notice here that, in addition to the OFAC sanctions we are learning about here, the U.S. Commerce Department's Bureau of Industry and Security (BIS) has "imposed restrictions on the export, reexport, and transfer (in country) of luxury goods to all end users in the Russian Federation (Russia) and Belarus and to certain Russian and Belarusian oligarchs and malign actors located worldwide."⁹

⁵ See, e.g., Kevin Granville, Eshe Nelson & Lananh Nguyen, Russia Appears to Have Avoided Default as it Makes a \$117 Million Bond Payment, NY Times (Mar. 17, 2022). JP Morgan was granted permission to process the payments, and sent the money to Citigroup's London office which made the payments to bondholders. *Id.*

⁶ See, e.g., IMF, Request for Purchase under the Rapid Financing Instrument and Cancellation of Stand-by Arrangement—Press Release; Staff Report; and Statement by the Executive Director for Ukraine, IMF Country Report No. 22/74 (Mar. 2022).

⁷ See, e.g., Ian Talley, Daniel Michaels & Jon Hilsenrath, How the U.S. and EU Cut Russia Off From the Global Economy, Wall Street Journal (Mar. 18, 2022).

⁸ But cf. Raquel Leslie & Brian Liu, Chinese Tech Companies Deepen Roots in Russia in Spite of U.S. Sanctions, Lawfare (Mar. 18, 2022).

⁹ Bureau of Industry and Security, Department of Commerce, Press Release, Commerce Restricts the Export of Luxury Goods to Russia and Belarus and to Russian and Belarusian Oligarchs and Malign Actors in Latest Response to Aggression Against Ukraine (Mar. 11, 2022); Bureau of Industry and

One issue with the OFAC sanctions relates to the complexity of the regime. Venezuelan sanctions were complex in similar ways, but the Russian sanctions are even more complex and have been evolving more rapidly: “the pace, volume and varying requirements of sanctions and other restrictions imposed after the invasion pose complex challenges for financial institutions, including cryptocurrency firms.”¹⁰ There is a risk that providers of compliance support services are not updating their blacklists quickly enough to ensure compliance.¹¹

If you visit the OFAC (Office of Foreign Assets Control) web pages you can find a page on Sanctions Programs and Country Information,¹² which includes links to a page on Ukraine-/Russia-related Sanctions,¹³ and another on Russian Harmful Foreign Activities Sanctions.¹⁴ Both pages includes measures that are relevant to the current situation. From both pages it is possible to sign up for email updates, and there are links to FAQs, as well as links to general information on OFAC, interpretive guidance and information about applying for a specific OFAC license for activities that would otherwise be subject to restrictions. In addition, there are General Licenses.

Executive Order 14024

A number of the recent sanctions actions have been carried out under Executive

Security, Department of Commerce, Imposition of Sanctions on ‘Luxury Goods’ Destined for Russia and Belarus and for Russian and Belarusian Oligarchs and Malign Actors Under the Export Administration Regulations (EAR), 87 Fed. Reg. 14785 (Mar. 16, 2022).

¹⁰ Mengqi Sun, Russia Sanctions Forcing Banks to Quickly Adapt, Wall Street Journal (Mar. 16, 2022)

¹¹ *Id.*

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<https://home.treasury.gov/policy-issues/financial-sanctions/sanctions-programs-and-country-information>.

¹³

<https://home.treasury.gov/policy-issues/financial-sanctions/sanctions-programs-and-country-information/ukraine-russia-related-sanctions>

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<https://home.treasury.gov/policy-issues/financial-sanctions/sanctions-programs-and-country-information/russian-harmful-foreign-activities-sanctions>.

Order 14024, issued in 2021.¹⁵ The EO states:

I, JOSEPH R. BIDEN JR., President of the United States of America, find that specified harmful foreign activities of the Government of the Russian Federation—in particular, efforts to undermine the conduct of free and fair democratic elections and democratic institutions in the United States and its allies and partners; to engage in and facilitate malicious cyber-enabled activities against the United States and its allies and partners; to foster and use transnational corruption to influence foreign governments; to pursue extraterritorial activities targeting dissidents or journalists; to undermine security in countries and regions important to United States national security; and to violate well- established principles of international law, including respect for the territorial integrity of states—constitute an unusual and extraordinary threat to the national security, foreign policy, and economy of the United States. I hereby declare a national emergency to deal with that threat.¹⁶

EO 14024 provides for the blocking of assets of persons to be specified that “come within the possession or control of any United States person.” A “person” is an individual or entity,¹⁷ and a United States person “means any United States citizen, lawful permanent resident, entity organized under the laws of the United States or any jurisdiction within the United States (including foreign branches), or any person in the United States.”¹⁸ The persons who may be subjected to the blocking sanctions include people who have been involved in interference with elections, transnational corruption, infliction of bodily harm on a US person or a citizen or national of a US ally or partner, actions to circumvent US sanctions including the use of digital currencies, material

¹⁵ Executive Order 14024 of April 15, 2021 Blocking Property With Respect To Specified Harmful Foreign Activities of the Government of the Russian Federation, 86 Fed. Reg. 20249 (Apr. 19, 2021). The EO cites the authority under which it is issued as “including the International Emergency Economic Powers Act (50 U.S.C. 1701 et seq.) (IEEPA), the National Emergencies Act (50 U.S.C. 1601 et seq.) (NEA), section 212(f) of the Immigration and Nationality Act of 1952 (8 U.S.C. 1182(f)), and section 301 of title 3, United States Code.” *Id.*

¹⁶ *Id.*

¹⁷ “[T]he term “entity” means a partnership, association, trust, joint venture, corporation, group, subgroup, or other organization.” *Id.* at §6.

¹⁸ *Id.*

assistance, sponsorship or financial support of any of the specified activities.¹⁹ The restrictions to apply to specified persons are prohibitions which “include” : “the making of any contribution or provision of funds, goods, or services by, to, or for the benefit of any person whose property and interests in property are blocked pursuant to this order; and.. the receipt of any contribution or provision of funds, goods, or services from any such person.”²⁰

As is typical in such Executive Orders, there are anti-evasion provisions which prohibit any “transaction that evades or avoids, has the purpose of evading or avoiding, causes a violation of, or attempts to violate any of the prohibitions set forth in this order” and conspiracies to violate the EO.²¹ Also typically EO 13024 also provides that no prior notice of any listing need be made because of the ability to transfer assets instantaneously.²²

IEEPA limits the ability of the President to prohibit donations to relieve human suffering, the limit does not apply where the President determines that the donations would seriously impair his ability to deal with the national emergency. EO 14024 makes such a determination.²³ EO 14024 does not prohibit transactions for the official business of the US federal government or of the United Nations.²⁴

EO 14024 was the basis for the imposition of sanctions measures against a number of Russian financial institutions, including Sberbank and VTB Bank (“which combined make up more than half of the total banking system in Russia by asset

¹⁹ EO 14024, § 1.

²⁰ *Id.* at § 2.

²¹ *Id.* at § 4.

²² *Id.* at § 7.

²³ *Id.* at § 5. (“I hereby determine that the making of donations of the types of articles specified in section 203(b)(2) of IEEPA (50 U.S.C. 1702(b)(2)) by, to, or for the benefit of any person whose property and interests in property are blocked pursuant to this order would seriously impair my ability to deal with the national emergency declared in this order, and I hereby prohibit such donations as provided by section 1 of this order.”)

²⁴ *Id.* at § 9.

value”), and Otkritie, Novikom, and Sovcom, together with subsidiaries.²⁵ The press release announcing the measures states that sanctioning VTB Bank “will sever a critical artery of Russia’s financial system. By imposing these sanctions, assets held in U.S. financial institutions will be instantly frozen and inaccessible to the Kremlin. This is one of the largest financial institutions Treasury has ever blocked and sends an unmistakable signal that the United States is following through on its promise of delivering severe economic costs.”²⁶

Directive 2 under EO 14024 specifies prohibitions imposed on US financial institutions with respect to the financial services sector of the Russian Federation Economy.²⁷ Unless provided by law or licensed or authorized by OFAC US financial institutions must not open or maintain correspondent accounts or payable-through accounts “for or on behalf of foreign financial institutions determined to be subject to the prohibitions of this Directive, or their property or interests in property,” and they must not process transactions for such foreign financial institutions.²⁸ A list of the relevant foreign financial institutions is attached as an annex to the Directive.²⁹ The Directive takes effect on March 26, 2022 (or for institutions later determined to be subject to the Directive, 30 days after that determination), thus allowing some time for the winding down of account relationships.³⁰ US financial institutions caught by the prohibition are: any U.S. entity (including its foreign branches) that is engaged in the business of accepting

²⁵ U.S. Treasury Press Release, U.S. Treasury Announces Unprecedented & Expansive Sanctions Against Russia, Imposing Swift and Severe Economic Costs (Feb. 24, 2022).

²⁶ *Id.*

²⁷ Directive 2 under E.O. 14024, Prohibitions Related to Correspondent or Payable-Through Accounts and Processing of Transactions Involving Certain Foreign Financial Institutions (Feb. 24, 2022) at https://home.treasury.gov/system/files/126/correspondent_accounts_directive_2.pdf.

²⁸ *Id.*

²⁹ *Id.* (“The Director of the Office of Foreign Assets Control, in consultation with the Department of State, has determined that, pursuant to section 1(a)(i) of the Order, the foreign financial institutions listed in Annex 1 to this Directive operate or have operated in the financial services sector of the Russian Federation economy, or are foreign financial institutions that are 50 percent or more owned, directly or indirectly, individually or in the aggregate, by one or more such foreign financial institutions, and are subject to the prohibitions of this Directive.”)

³⁰ *Id.*

deposits, making, granting, transferring, holding, or brokering loans or credits, or 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 U.S. holding companies, U.S. affiliates, or U.S. subsidiaries of any of the foregoing. This term includes those branches, offices, and agencies of foreign financial institutions that are located in the United States, but not such institutions' foreign branches, offices, or agencies.³¹ A correspondent account is "an account established by a U.S. financial institution for a foreign financial institution to receive deposits from, or to make payments on behalf of, the foreign financial institution, or to handle other financial transactions related to such foreign financial institution."³² A payable- through account is "a correspondent account maintained by a U.S. financial institution for a foreign financial institution by means of which the foreign financial institution permits its customers to engage, either directly or through a subaccount, in banking activities usual in connection with the business of banking in the United States."³³

Directive 3 under EO 14024, issued on the same date as Directive 2, prohibits transactions and dealings by U.S. persons or within the United States in new debt of longer than 14 days maturity and new equity of Russian state-owned enterprises, entities that operate in the financial services sector of the Russian Federation economy, and other entities determined to be subject to the prohibitions in the directive.³⁴ Sberbank, Gazprombank, Gazprom and Transneft are among the entities subject to

³¹ *Id.*

³² *Id.*

³³ *Id.*

³⁴ Directive 3 under E.O. 14024, Prohibitions Related to New Debt and Equity of Certain Russia-related Entities (Feb. 24, 2022) available at https://home.treasury.gov/system/files/126/new_debt_and_equity_directive_3.pdf.

these measures.³⁵

On February 28 Directive 4 under Executive Order 14024 prohibited transactions by a US person “involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, or the Ministry of Finance of the Russian Federation, including any transfer of assets to such entities or any foreign exchange transaction for or on behalf of such entities.”³⁶

OFAC has also issued a number of General Licenses authorizing certain transactions relating, for example, to winding down transactions of blocked persons and certain debt, equity and derivatives transactions. For example, General License No. 11 allowed transactions incident and necessary to the wind down of transactions involving specified blocked persons including VTB Bank.³⁷

Executive Orders 14066, 14068

Executive Order 14066 prohibits the import of fossil fuels from Russia to the US, and new investment in the energy sector in Russia, and “any approval, financing, facilitation, or guarantee by a United States person, wherever located, of a transaction by a foreign person where the transaction by that foreign person would be prohibited by this section if performed by a United States person or within the United States.”³⁸ General License 16 allowed imports of fossil fuels pursuant to contracts entered into before March 8, 2022 up to April 22, 2022.³⁹

³⁵ *Id.*

³⁶ Directive 4 under E.O. 14024, Prohibitions Related to Transactions Involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, and the Ministry of Finance of the Russian Federation (Feb. 28, 2022) at https://home.treasury.gov/system/files/126/eo14024_directive_4_02282022.pdf.

³⁷ General License No. 11, Authorizing the Wind Down of Transactions Involving Certain Blocked Persons (Feb. 24, 2022).

³⁸ Executive Order 14066 of March 8, 2022 Prohibiting Certain Imports and New Investments With Respect to Continued Russian Federation Efforts To Undermine the Sovereignty and Territorial Integrity of Ukraine, 87 Fed Reg. 13625 (Mar. 10, 2022).

³⁹ General License No. 16, Authorizing Transactions Related to Certain Imports Prohibited by Executive Order of March 8, 2022 Prohibiting Certain Imports and New Investments With Respect to Continued Russian Federation Efforts to Undermine the Sovereignty and Territorial Integrity of

Executive Order 14068 prohibits certain imports into Russia and from Russia into the US, together with new investments in any sector of the Russian economy specified by the Secretary of the Treasury, supply of US dollar banknotes to Russia, and “any approval, financing, facilitation, or guarantee by a United States person, wherever located, of a transaction by a foreign person where the transaction by that foreign person would be prohibited by this section if performed by a United States person or within the United States.”⁴⁰ General License No. 18 allows noncommercial personal remittances between US persons and individuals in Russia.⁴¹

LOBBYING AND SANCTIONS

Sanctions measures are not generally subject to notice and comment rule-making as many administrative actions are, and nor are they subject to a legislative process. Congress does sometimes legislate for sanctions measures as we have seen, and regulations are adopted with respect to sanctions measures, which aids transparency.⁴² However, as sanctions measures are rolled out, especially in the context of a crisis, there is significant uncertainty. And although this section of our materials focuses on the US sanctions on Russia, bear in mind that some financial institutions are going to need to comply with sanctions measures imposed in different jurisdictions. There are times when there are significant divergences between approaches in different jurisdictions as we saw in section 1 of the sanctions materials (the EU blocking regulation).

For many reasons sanctions measures may seem to be unpredictable, in terms of whether and when sanctions measures may be imposed and by what countries, and also in terms of the scope and content of the sanctions measures. Measures

Ukraine (Mar. 8, 2022).

⁴⁰ Executive Order 14068 of March 11, 2022 Prohibiting Certain Imports, Exports, and New Investment With Respect to Continued Russian Federation Aggression, 87 Fed. Reg. 14381 (Mar. 15, 2022).

⁴¹ General License No. 18, Authorizing U.S. Dollar-Denominated Banknote Noncommercial, Personal Remittances Prohibited by Executive Order of March 11, 2022 (Mar. 11, 2022).

⁴² Office of Foreign Assets Control, Russian Harmful Foreign Activities Sanctions Regulations, 87 Fed. Reg. 11297 (Mar. 1, 2022) codified at 31 CFR Part 587.

sometimes specify that it is not necessary to warn targets of the measures in advance. But we have also seen that sometimes sanctions measures are designed to apply as of some future time, in particular when the interests of US businesses and people are going to be affected. But a process for developing sanctions measures that lacks transparency also risks unanticipated effects.

We have discussed the idea that sanctions measures may have adverse impacts on the populations of countries targeted for sanctions measures, either because the sanctions measures are designed to be very broad, or are unthinkingly broad, or because there is over-compliance (derisking) because of concerns about enforcement action. Human Rights Groups campaign to limit the harmful impact of sanctions measures.⁴³

Businesses that are adversely affected by sanctions measures may apply for a license, or may lobby to have the sanctions amended more generally. But targeted countries and businesses also engage in lobbying. In May 2020 a complaint was filed by a PDVSA entity against David Rivera's consulting firm alleging that a contract under which he was to be paid \$50m for "strategic consulting services" had been breached when he provided only 5 pages of reports.⁴⁴ News articles suggest this was only part of Venezuela's lobbying efforts.⁴⁵

Lobbying activities may constitute a violation of sanctions measures.⁴⁶

SANCTIONS COMPLIANCE AND ENFORCEMENT

It is one thing to adopt sanctions measures, and another to enforce compliance with those measures. Countries that do not adopt sanctions measures with respect to a

⁴³ See, e.g., Human Rights Watch, Myanmar, Sanctions, and Human Rights (Feb. 18, 2021).

⁴⁴ Complaint in PDV USA Inc. V InterAmerican Consulting Inc, Case 20-cv-3699, SDNY. See also Patricia Mazzei, Venezuelan Oil Company Sues Miami Ex-Congressman Over \$50 Million Deal, NY Times (May 12, 2020).

⁴⁵ Antonio Maria Delgado & Jay Weaver, Rivera is the tip of the iceberg; Citgo had 'multiple' lobbying contracts, sources say, Miami Herald (Jun. 4, 2020); Alex Gangitano, Maduro ally hires lobbyist to ease US sanctions, The Hill (Jan. 27, 2020).

⁴⁶ See, e.g., OFAC Press Release, Settlement Agreement between the U.S. Department of the Treasury's Office of Foreign Assets Control and Park Strategies, LLC (Jan. 21, 2020).

particular situation may help sanctioned countries minimize the impact of sanctions measures. For example, Russia and China helped Venezuela.⁴⁷ The EU helped Iran with respect to US sanctions as we have seen. But Iran also developed its own system for avoiding sanctions:

the clandestine banking system works like this: Iranian banks that serve companies barred by U.S. sanctions from exporting or importing engage affiliate firms in Iran to manage sanctioned trade on their behalf. Those firms establish companies outside of Iran's borders to serve as proxies for the Iranian traders. The proxies trade with foreign purchasers of Iranian oil and other commodities, or sellers of goods for import into Iran, in dollars, euros or other foreign currencies, through accounts set up in foreign banks.

Some of the revenue is smuggled into Iran by couriers who carry cash withdrawn from the proxy company accounts abroad, according to some of the officials. But much of it remains in bank accounts abroad, according to the Western officials. The Iranian importers and exporters trade foreign currency among themselves, on ledgers maintained in Iran, according to the Iranian central bank.⁴⁸

Enforcement of sanctions against Russia is an especially complex task.⁴⁹ A number of US agencies will play a role in enforcing compliance, including the IRS, as noted above, and various financial regulators. FinCEN has issued an alert with respect to potential evasion of sanctions.⁵⁰

Making sure to comply with the rules is complicated.⁵¹ If lists of designated persons and details of the rules change, then compliance needs to respond to the

⁴⁷ See, e.g., Daphne Psaledakis & Humeysa Pamuk, U.S. blacklists second unit of Russia's Rosneft over Venezuela oil, Reuters (Mar. 12, 2020).

⁴⁸ Ian Talley, Clandestine Finance System Helped Iran Withstand Sanctions Crush, Documents Show, Wall Street Journal (Mar. 18, 2022).

⁴⁹ Norman Eisen, Robin J. Lewis, Aaron Klein, Lilly Blumenthal, Mario Picon, Scott Johnston & Charlie Loudon, Mapping financial countermeasures against Russian aggression: Introducing the Brookings Sanctions Tracker, Brookings (Mar. 14, 2022) ("The task the world's democracies have set for themselves is not easy. Effectively sanctioning a nation as large and interconnected as Russia is difficult.")

⁵⁰ FinCEN, FinCEN Advises Increased Vigilance for Potential Russian Sanctions Evasion Attempts, FIN-2022-Alert001 (Mar. 7, 2022).

⁵¹ See, e.g., Mengqi Sun, Evolving Venezuela Sanctions Pose Problems for Banks, WSJ (Feb 25, 2019).

changes, which can be complicated. A PWC publication states:

The process of complying with watch list filtering requirements would seem to be straightforward: financial institutions have to screen the names of individuals and entities on various lists and, depending on the list and the entity, decline business with potential customers or conduct enhanced due diligence. But the reality is far more complicated. Even institutions with relatively mature screening programs can find themselves struggling to align their programs quickly enough with a highly mutable and ever-more-complex policy and regulatory environment.⁵²

The information in this section relates to sanctions involving one country and where the US and the EU and some other countries have co-ordinated their actions. Imagine a financial institution faced with a proposed transaction involving multiple different jurisdictions trying to make sure to comply with all of the relevant sanctions regimes. A number of businesses offer technological assistance for compliance with these requirements.⁵³

In a **Joint Fact Sheet on Foreign Correspondent Banking**, US federal banking agencies (FBAs) described their expectations of US financial institutions in their relationships with foreign financial institutions (FFIs) as follows:

The FBAs expect U.S. depository institutions to have robust BSA and OFAC compliance programs that include appropriate customer due diligence so that the institutions have a clear understanding of FFI risk profiles and expected account activity. This information helps U.S. depository institutions make informed decisions regarding the risks associated with their FFI relationships and the level and nature of suspicious activity monitoring needed to manage those risks effectively. In order for U.S. depository institutions to develop a clear understanding of FFI risk profiles and determine how best to manage the risks associated with these relationships, they are expected to obtain and review sufficient information about their FFI relationships, including the types of customers the FFI serves and the markets in which the FFI is active. This approach allows the U.S. depository institution to conduct an adequate assessment of the risks present in: (i) the FFI's business and markets, (ii) the type, purpose and anticipated activity, (iii)

⁵² PWC, Name, Set, Match Enhancing Watch List Screening Through Analytics (Apr. 2016).

⁵³ See, e.g., Deloitte, RegTech Universe at <https://www2.deloitte.com/lu/en/pages/technology/articles/regtech-companies-compliance.html>; SWIFT Sanctions Screening at <https://www.swift.com/our-solutions/compliance-and-shared-services/financial-crime-compliance/sanctions-screening>.

the nature and duration of the relationship with the FFI, and (iv) the supervisory regime of the jurisdiction in which the FFI is licensed, and to design and implement controls to manage these risks effectively. Under existing U.S. regulations, there is no general requirement for U.S. depository institutions to conduct due diligence on an FFI's customers. In determining the appropriate level of due diligence necessary for an FFI relationship, U.S. depository institutions should consider the extent to which information related to the FFI's markets and types of customers is necessary to assess the risks posed by the relationship, satisfy the institution's obligations to detect and report suspicious activity, and comply with U.S. economic sanctions. This may require U.S. depository institutions to request additional information concerning the activity underlying the FFI's transactions in accordance with the suspicious activity reporting rules and sanctions compliance obligations....

Enforcement actions by the FBAs are an extension of the supervisory process and are used to address more serious deficiencies, or situations where deficiencies have not been corrected in the course of the supervisory process. Enforcement actions reinforce awareness of senior management and boards of directors of the deficiencies identified during the supervisory process and ensure they take prompt remedial actions to correct the identified deficiencies. Enforcement tools may vary and can include informal memoranda of understanding, or formal, public, written agreements, and cease-and-desist orders. The FBAs are required by statute to use their cease-and-desist authority when an institution fails to establish or maintain a BSA compliance program or fails to correct any problem with the program previously reported to the institution. In very limited instances, when corrective action has not been achieved within a reasonable amount of time or serious violations or unsafe or unsound practices or breaches of fiduciary duty have been identified, the FBAs also have the authority to assess civil money penalties (CMPs). CMPs are designed by statute to serve as a deterrent to future violations, practices or breaches of fiduciary duty, to encourage correction of violations, practices or breaches of fiduciary duty, and in the case of individual actions, to emphasize the accountability of individuals...

OFAC administers and enforces the U.S. economic and trade sanctions programs based on U.S. foreign policy and national security threats. In cases where institutions are supervised by the FBAs, the FBAs examine for BSA/AML and OFAC compliance, and in situations involving apparent BSA/AML or sanctions violations resulting from deficiencies, FinCEN and OFAC coordinate with the FBAs. In determining whether an enforcement action is appropriate, FinCEN considers whether the institution responded adequately to the FBA's previous corrective actions or if the institution engaged in significant violations. Similarly, in certain circumstances, OFAC will consult with relevant FBAs regarding the quality and effectiveness of

an institution's compliance program when determining the appropriate enforcement response. OFAC investigates cases of sanctions violations, many of which (over 95 percent) are closed with administrative measures such as cautionary or no action letters. This means that less than five percent of all cases of sanctions-related violations investigated by OFAC have resulted in a civil monetary penalty or other public enforcement response.⁵⁴

In November 2018 OFAC announced a settlement with Société Générale, a French bank, for \$53,966,916.05 with respect to apparent sanctions violations under the Cuban Assets Control Regulations, the Iranian Transactions and Sanctions Regulations, and the Sudanese Sanctions Regulations.⁵⁵ In addition the bank entered into deferred prosecution agreements with the U.S Attorney's Office of the Southern District of New York and the New York County District Attorney's Office, and a separate agreement with agreement with the New York State Department of Financial Services. In total Société Générale agreed to pay \$1.3 billion.⁵⁶ OFAC noted that Société Générale processed 1,077 transactions totaling \$5,560,452,994.36 in apparent violation of sanctions. The Settlement agreement noted the voluntary disclosure of the apparent violations which were characterized as egregious.⁵⁷ Société Générale:

... certain business lines of SG processed non-transparent payments involving the removal, omission, obscurement, or failure to include references to sanctioned parties in transactions processed to or through the United States or U.S. financial institutions. SG also had documented procedures on how to omit sanctioned parties on payment instructions destined for or transiting the United States. While some of the conduct that led to the apparent violations is specific to a particular branch and/or business line of SG (as described in detail below), several

⁵⁴ U.S. Department of the Treasury and Federal Banking Agencies, Joint Fact Sheet on Foreign Correspondent Banking: Approach to BSA/AML and OFAC Sanctions Supervision and Enforcement (Aug. 30, 2016)

⁵⁵ See US Department of the Treasury Press Release, Settlement Agreement between the U.S. Department of the Treasury's Office of Foreign Assets Control and Société Générale S.A. (Nov. 19, 2018).

⁵⁶ Société Générale Press Release, Société Générale Reaches Agreements with U.S. Authorities to Resolve U.S. Economic Sanctions and AML Investigations (Nov. 19, 2018).

⁵⁷ Settlement Agreement between the U.S. Department of the Treasury's Office of Foreign Assets Control and Société Générale S.A. (Nov. 19, 2018) at https://home.treasury.gov/system/files/126/20181118_socgen.pdf.

components of SG appear to have engaged in similar conduct that resulted in apparent violation of, rather than compliance with, OFAC sanctions regulations. In addition, while SG implemented sanctions compliance measures prior to and during the review period, several units of SG did not receive guidance at the time and continued to process transactions in apparent violation of OFAC sanctions... At various points in 2003 and 2004, certain SG personnel circulated procedures for processing payments for parties located in embargoed countries by omitting the parties' names from the payment messages sent to U.S. financial institutions. In November 2003, a member of the Treasury Desk and Money Market Back Office (MMBO) within SG CIB received a memo entitled "Scheme for international settlement with countries under USD embargo," which described how to process different transactions for customers located in embargoed countries... Beginning in mid-2004, various units within SG began undertaking a number of efforts to improve sanctions compliance at the bank, partly in response to certain U.S. government enforcement actions against non-U.S. banks for sanctions-related violations, and years before several other significant enforcement actions against non-U.S. banks. SG's compliance efforts included providing trainings, circulating compliance messages, and updating policies and procedures. Despite these efforts, certain SG personnel continued to process transactions in violation of the applicable OFAC sanctions, including by removing references to OFAC-sanctioned parties in the payment instructions sent to U.S. financial institutions... SG's [Paris Rive Gauche PRGE] branch [of SG's retail banking division in France, Banque de Detail enFrance BDDF], originated a number of payments on behalf of the Sudanese Entity. In particular, from at least May 2, 2007 through November 27, 2008, SG's PRGE branch originated SWIFT payment messages for the Sudanese Entity that used the company's French mailing address, rather than the Sudanese physical address in BDDF's client database. Because the messages did not contain references to any OFAC-sanctioned country or party, they were not flagged by BDDF's automated OFAC interdiction filter for review... From December 4, 2008 through January 16, 2009, BDDF's payment message system automatically populated seven payment messages with the Sudanese Entity's Sudanese address, after someone at the PRGE branch's Middle Office had flagged in the database that mail sent to the Sudanese Entity's French address had been returned as undeliverable. BDDF's automated OFAC interdiction filter stopped all seven payments for review, and, at the direction of a senior member of the PRGE branch's Back Office, Back Office employees at the PRGE branch manually resubmitted four payments to change the Sudanese Entity's Sudanese address to the company's French address.⁵⁸

⁵⁸ *Id.*

This case is an example of a case that led financial institutions to be more concerned about compliance issues.

In February 2019 OFAC announced that it was identifying an individual based in Turkey as a foreign sanctions evader, the first time it had taken such action against an individual:

“Treasury is sanctioning Kayakiran not just for his willful violation of U.S. sanctions on Iran, but also for directing staff to commit and cover up these illegal acts. This is the first time that OFAC has designated an individual as a Foreign Sanctions Evader while resolving an enforcement matter, and is a marked change to how we will counter these acts of deception,” said Sigal Mandelker, Treasury Under Secretary for Terrorism and Financial Intelligence. “This action is a clear warning that anyone in supervisory or managerial positions who directs staff to provide services, falsify records, commit fraud, or obstruct an investigation into sanctions violations exposes themselves to serious personal risk.”⁵⁹

These two examples illustrate sanctions enforcement against foreign persons and entities. Bryan Early and Keith Preble have traced an evolution of US sanctions enforcement from a strategy of focusing on catching a large number of violators to taking a smaller number of bigger enforcement actions (they describe this as a change from fishing to whale-hunting).⁶⁰ They argue that the whale-hunting strategy is more effective in obtaining compliance. On the targeting of foreign firms they write: So, why are foreign banks responsible for all of OFAC’s largest penalties? For years, many foreign banks ignored or deliberately violated US sanctions provisions. When financial institutions flout US sanctions requirements, the volume of transactions they engage in can mean they engage in hundreds or even thousands of distinct sanctions violations. This volume makes such entities lucrative enforcement targets for OFAC and US criminal enforcement bodies, as those violators may have engaged in thousands of transactions subject to maximum statutory penalties. Foreign banks not only have the resources to pay the enormous fines, but they also have strong incentives to settle those liabilities rather than risk being denied access to

⁵⁹ US Department of the Treasury, Treasury Sanctions Turkish National as Foreign Sanctions Evader Due To Repeated Violations of U.S. Sanctions Against Iran (Feb. 7, 2019).

⁶⁰ Bryan R. Early & Keith A. Preble, Enforcing US Economic Sanctions: Why Whale Hunting Works, 43:1 The Washington Quarterly 159-175 (2020).

the US financial system. While lucrative, pursuing these “whale” cases requires significant resources and expertise to pursue.

Not all enforcement actions relate to large value or wilful violations. In January 2022, Airbnb Payments entered into a settlement with OFAC with respect to Cuba sanctions infringed when Airbnb set up business in Cuba “without fully addressing the complexities of operating a Cuba-related sanctions compliance program for internet-based travel services,” and “the scaling up of its services in Cuba appears to have outpaced the company’s ability to manage the associated sanctions risks via its technology platforms.”⁶¹ The payments processed by Airbnb that violated sanctions related to travel outside the permitted categories authorized by OFAC. Individual payment amounts were small.

In December 2021, TD Bank NA settled with OFAC in circumstances that illustrate some of the compliance issues mentioned above:

Between December 20, 2016 and August 15, 2018, TDBNA processed 1,479 transactions totaling \$382,685.38, and maintained nine accounts on behalf of five employees of the North Korean mission to the United Nations without a license from OFAC. At account opening, the account holders of all nine accounts presented to TDBNA North Korean passports. However, these passports did not generate an alert during the customer screening process because TDBNA relied heavily on a vendor-supplied Politically Exposed Persons (PEP) list (“PEP list”), which did not include government employees of sanctioned countries. In addition, TDBNA employees often misidentified North Korea (referring to it as Korea or South Korea or using a country code meant for South Korea), or left the citizenship field blank in the customer profiles. As a result, TDBNA’s screening system did not flag any of these accounts because the citizenship information was missing or incorrect.

Under the North Korea Sanctions Regulations (NKSr), 31 C.F.R. § 510.510(c), a general license authorizing certain transactions with the North Korean Mission to the United Nations specifies that it does not authorize U.S. financial institutions to open and operate accounts for employees of the North Korean mission. It further specifies that U.S. financial institutions are required to obtain OFAC specific licenses to operate accounts for such persons. Because TDBNA did not have a specific license to provide these services, its conduct resulted in the

⁶¹ OFAC Settles with Airbnb Payments, Inc. for \$91,172.29 Related to Apparent Violations of the Cuban Assets Control Regulations, Enforcement Release (Jan.3, 2022).

apparent violations of 31 C.F.R. § 510.201.⁶²

Similarly, Payoneer, an online money transmitter based in New York, settled with OFAC in 2021 for conduct that involved compliance deficiencies rather than wilful violation of sanctions:

Between February 4, 2013 and February 20, 2018, Payoneer processed 2,220 transactions totaling \$793,950.70 in apparent violation of multiple OFAC-administered sanctions programs (the “Apparent Violations”). Payoneer’s policies and procedures dating back as far as June 2015 specified that transactions involving parties in sanctioned locations were prohibited, but the testing and auditing conducted to verify that these policies and procedures were being implemented failed to identify the compliance deficiencies that led to the Apparent Violations. The Apparent Violations, which related to commercial transactions processed by Payoneer on behalf of its corporate customers and card-issuing financial institutions, resulted from multiple sanctions compliance control breakdowns, including (i) weak algorithms that allowed close matches to SDN List entries not to be flagged by its filter, (ii) failure to screen for Business Identifier Codes (BICs) even when SDN List entries contained them, (iii) during backlog periods, allowing flagged and pended payments to be automatically released without review, and (iv) lack of focus on sanctioned locations, especially Crimea, because it was not monitoring IP addresses or flagging addresses in sanctioned locations.

These compliance deficiencies resulted in apparent violations of Section 1(a)(iii) and Section 2 of Executive Order 13685 of December 19, 2014, “Blocking Property of Certain Persons and Prohibiting Certain Transactions with Respect to the Crimea Region of Ukraine”; the Zimbabwe Sanctions Regulations, 31 C.F.R. § 541.201; the Weapons of Mass Destruction Proliferators Sanctions Regulations, 31 C.F.R. § 544.201; the Iranian Transactions and Sanctions Regulations, 31 C.F.R. § 560.204; the now-repealed Sudanese Sanctions Regulations (SSR), 31 C.F.R. §538.205; and the Syrian Sanctions Regulations, 31 C.F.R. § 542.207.⁶³

Financial firms are particularly vulnerable to large fines as the fines are calculated for each apparent violation and financial firms engage in many more

⁶² OFAC Settles with TD Bank, N.A. for \$115,005.04 Related to Apparent Violations of the North Korea Sanctions Regulations and the Foreign Narcotics Kingpin Sanctions Regulations, Enforcement Release (Dec. 23, 2021).

⁶³ OFAC Enters Into \$1,385,901.40 Settlement with Payoneer Inc. for Apparent Violations of Multiple Sanctions Programs, Enforcement Release (Jul. 23, 2021).

transactions that may involve violations than non-financial corporations. These two recent actions illustrate that non-bank payments processors also need to be concerned about sanctions compliance.