

UK UPDATE: RUSSIA SANCTIONS

The UK, working with its allies and partners, has imposed a series of sanctions aimed at encouraging Russia to cease actions threatening the territorial integrity, sovereignty and independence of Ukraine. This is the first time post-Brexit that a major set of trade sanctions are emanating from Brussels and London separately, as detailed in our earlier alert.¹

The currently existing UK measures can, in part, be traced back to the sanctions put in place when the UK was a member of the EU² and reflected in UK statute³. As part of the new UK sanctions powers, amendments to the governing regulations were made on 10 February which broadened the scope of the designation criteria, enabling the UK to more readily designate a greater number of individuals and businesses associated with the Kremlin.⁴ These therefore moved the UK position further from the EU regulations currently in force.

The latest UK measures can be divided into several areas, as set out below.

Asset freezes and blocking sanctions

The UK has this week imposed asset freezes and blocking sanctions on a large number of specific banks (such as VTB, Russia's second-largest bank),⁵ high-net worth individuals and leading members of the Russian elite (including President Putin and Foreign Minister Lavrov),⁶ and certain companies (Rostec for example, Russia's biggest defence company) and members of the Duma and Federation council.⁷

There are an increasing cascade of designations being updated by the government,⁸ as well as a pro-active trend of self-exclusion by individuals who may potentially be targeted in the future, and are now seeking to divest themselves of interests.

The Foreign Secretary, Liz Truss, announced that the UK plans to publish a "hit list" of Russian high net worth individuals with overseas assets to be targeted. This is a legally complex area and it is reported that some individuals at risk of being singled out have already contacted the Foreign Office threatening legal action against any sanctions decision.

¹ Gide Loyrette Nouel's recent Europe briefing on sanctions sets out the various EU measures, <https://www.gide.com/fr/actualites/sanctions-targeting-russia-in-response-to-the-crisis-in-ukraine-update>

² This includes principally Regulations (EU) No 269/2014, No 692/2014 and No 833/2014.

³ Russia (Sanctions) (EU Exit) Regulations 2019 (SI, 2019, No. 855).

⁴ Russia (Sanctions) (EU Exit) (Amendment) Regulations 2022 (SI, 2022, No. 123).

⁵ Russia Financial Sanctions Notice, 24 February 2022.

⁶ Russia Financial Sanctions Notice, 25 February 2022.

⁷ Current list of designated persons: Russia, available at:

https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1058111/Russia.pdf

⁸ The people, entities and ships designated or specified under regulations made under the Sanctions and Anti-Money Laundering Act 2018 are detailed in the UK Sanctions List, available at: <https://www.gov.uk/government/publications/the-uk-sanctions-list#full-publication-update-history>

On 1 March 2022, Bob Seely MP went to the length of naming individual solicitors at named law firms working for individuals and entities close to the Russian state in the Commons⁹, highlighting the growing reputational risk of working with Russian state actors.

Financial sanctions

A number of financial measures have been introduced to restrict Russian access to finance through the UK.

The Russia (Sanctions) (EU Exit) (Amendment) (No 2) Regulations 2022 came into force on 1 March 2022,¹⁰ amending the existing sanctions prohibiting dealing with transferable securities or money-making instruments.

The scope of the existing prohibitions has been extended to widen the scope of dealing with securities or money-market instruments issued across sectors of the Russian economy. The legislation also prohibits dealing in Russian sovereign debt issued on or after 1 March. This is part of the proposals by the UK to cut off Russian state access to financial resources through the UK economy.

Access to UK finance

Specifically this instrument extends existing restrictions prohibiting the issuing of loans or credit, such that¹¹:

- the prohibitions apply to loans and credit issued to a person connected with Russia¹² as well as those owned by a such persons or those acting on their behalf or at their direction (which is aimed at circumvention);
- the prohibitions apply to loans and credit provided to the Government of Russia; and
- the scope of the existing prohibitions is expanded to apply to loans and credit provided to entities incorporated or constituted under UK law which are owned by sectorally-sanctioned entities.

Clearing and Settlement in Pounds Sterling

The Russia (Sanctions) (EU Exit) (Amendment) (No 2) Regulations 2022 additionally introduced a new measure to prohibit a UK credit or financial institution from establishing or continuing a correspondent banking relationship and from processing sterling payments to, from or via a designated person or a credit or financial institution owned or controlled by them.

As the "processing" of a sterling payment includes the clearing and settlement of such a payment wherever they emanate from, this measure has an extra-territorial effect. There is therefore potential for transactions denominated in Sterling, but with no UK nexus, to be caught

⁹ See Hansard, volume 709, Tuesday 1 March 2022

¹⁰ Russia (Sanctions) (EU Exit) (Amendment) (No 2) Regulations 2022 (SI, 2022, No. 194).

¹¹ As listed in Schedule 2 to the Russia (Sanctions) (EU Exit) Regulations 2019 (SI, 2019, No. 855).

¹² As defined in Regulation 19A(2) of the Russia (Sanctions) (EU Exit) Regulations 2019 (SI, 2019, No. 855).

and funds seized, in a manner similar to OFAC's operation of sanctions regimes with Cuba and Iran, for example.

Trade restrictions

New restrictions on Russian ships came into force on 1 March 2022, by way of the Russia (Sanctions) (EU Exit) (Amendment) (No. 4) Regulations 2022.¹³

- prohibiting Russian ships, and other ships specified by the Secretary of State, from entering ports in the United Kingdom;
- conferring powers on the Secretary of State to give movement or detention directions; and
- prohibiting the registration of ships on the UK Ship Register where they are owned, controlled, chartered or operated by a designated person or persons connected with Russia, or where they are a specified ship.

These shipping sanctions could lead to genuine cases of impossibility of performance under the law of frustration (in addition to the force majeure claims that were seen during the Covid-19 pandemic as a result of government restrictions), which would be a highly unusual legal development.

Foreign exchange

Finally, the Russia (Sanctions) (EU Exit) (Amendment) (No. 5) Regulations 2022 (in force from 1 March 2022)¹⁴ prohibit the provision of financial services for the purpose of foreign exchange reserve and asset management to the following:

- the Central Bank of the Russian Federation;
- the National Wealth Fund of the Russian Federation;
- the Ministry of Finance of the Russian Federation;
- a person owned or controlled (directly or indirectly) by any of the above; or
- a person acting on behalf of or at the direction of any of the above.

“Foreign exchange reserve and asset management” means activities relating to the reserves or assets of the above persons, including:

- money market instruments;
- foreign exchange;
- derivative products (including futures and options);
- exchange rate and interest rate instruments (including products such as swaps and forward rate agreements); transferable securities; other negotiable instruments and financial assets (including bullion); and
- special drawing rights.

¹³ Russia (Sanctions) (EU Exit) (Amendment) (No. 4) Regulations 2022 (SI, 2022, No. 203).

¹⁴ Russia (Sanctions) (EU Exit) (Amendment) (No. 5) Regulations 2022 (SI, 2022, No. 205).

General licences

The UK's Office of Financial Sanctions Implementation (OFSI) has published a number of Russia-related general licences¹⁵ to help financial institutions deal with issues raised by sanctions, for example those licences allowing transactions with certain sanctioned entities to be wound down.¹⁶ Taking these actions within the time frames allowed by each general licence is the responsibility of the parties affected, outside of which they will be non-compliant and subject to penalties.

The UK's approach is similar to the Office of Foreign Assets Control (OFAC) in the US, providing exemptions in general licences to allow certain activity that would otherwise be prohibited by financial sanctions. A special licence may be needed where activity is not covered by a general licence.

This is a fast-moving area - seven general licences have been issued since 25 February 2022 - and companies should be vigilant to changes that may arise (e.g. with respect to the trade in petroleum and gas products under General Licence INT/2022/1277877).

Export control

The UK has implemented punitive new restrictions on trade and export controls against Russia's hi-tech and strategic industries, such as electronics, telecommunications, and aerospace, similar to those implemented by the EU and the US.

On 1 March 2022, the Export Control Joint Unit issued a notice to inform exporters of the immediate suspension of extant licenses for the export of all dual-use items to Russia.¹⁷

Another statutory instrument which came into force on 1 March 2022, the Russia (Sanctions) (EU Exit) (Amendment) (No. 3) Regulations 2022,¹⁸ expanded the existing restrictions applicable to military and dual-use items.

This legislation prohibits the export supply and delivery, making available and transfer of dual-use items and critical industry items to, or for use in, Russia, irrespective of end-user. This restriction further extends to the provision of related technical assistance, financial services, funds and brokering services.¹⁹

As we learned from the experience of enforcement under the Iran sanctions, the list of products that are potentially dual-use can be extremely wide. These restrictions therefore have the potential to be extremely far reaching in catching a wide range of technology which may not appear to be restricted at first glance and each company should have a compliance policy in place for monitoring of whole group activity in this regard.

¹⁵ General Licence INT/2022/1277777; General Licence INT/2022/1277778; General Licence INT/2022/1277877.

¹⁶ General Licence INT/2022/1272278; General Licence INT/2022/1280976; General Licence INT/2022/1280876I; General Licence NT/2022/1295476.

¹⁷ Notice to Exporters 2022/03: licence suspensions and OGELs revised, available at: <https://www.gov.uk/government/publications/notice-to-exporters-202203-licence-suspensions-and-ogels-revised/nte-202203-licence-suspensions-and-ogels-revised>

¹⁸ Russia (Sanctions) (EU Exit) (Amendment) (No. 3) Regulations 2022 (SI, 2022, No. 195).

¹⁹ "Critical industry goods" includes the software and technology specified in Schedule 2A to the (No.3) Regulations, Schedule 2 or 3 to the Export Control Order 2008, or Annex I of the EU Dual-Use Regulation.

Economic Crime (Transparency and Enforcement) Bill

Measures on unexplained wealth orders have been brought forward, with the early publication of the Economic Crime (Transparency and Enforcement) Bill on 28 February 2022. Further detail is provided on reforms to Companies House and a register of overseas property ownership. On publication of the Economic Crime (Transparency and Enforcement) Bill, the government referenced the upcoming publication of a white paper detailing plans to set up a new dedicated 'kleptocracy Cell' in the National Crime Agency to target sanctions evasion and corrupt Russian assets hidden in the UK.

This is partly in response to the criticism of the government for not acting more widely against those with assets in the UK or controlled overseas through UK tax domicile status.

Russian counter-measures

Whilst Russia is yet to announce its full counter-measures in direct response, but it can be expected that this is a real possibility - in 2014 Russia imposed special economic measures against countries that introduced sanctions against Russia, and in September 2021 President Putin extended these measures until 31 December 2022.

There are reports that Russia may legislate to allow Russian entities to ignore arbitration clauses in their private contracts and refer disputes to Russian courts. There is also a risk of measures under Russian law becoming applicable that could breach UK sanctions for the Russian subsidiary's UK parent (e.g. capitalisation requirements that fall outside the UK general licences). Companies will therefore need to take counsel in the affected jurisdictions and, in the case of Russia, check whether this is covered by a general licence (e.g. General Licence INT/2022/1280876 allows UK legal persons to pay legal fees and insurance premiums in respect of maintaining subsidiaries basic needs).

What's next for companies?

Following the rapid developments and increasing numbers of sanctions imposed, commercial groups with operations in the UK will have an evolving compliance position to monitor. There are a number of specific areas where companies may need to pay particular attention, for example:

- when unwinding portfolios of investments that have the effect of providing finance to sanctioned entities, including derivatives transactions and close out payments;
- where joint ventures involving affected assets (e.g. real estate, stocks and shares) need to be isolated or divested and need lead time to achieve this;
- where preparation for sanctions with extra-territorial effect (e.g. currency clearing or US secondary sanctions) may involve significant operational challenges in international groups (such as isolating group operational functions like IT, accounting, e-mail and other corporate services) and the monitoring of the activities of overseas subsidiaries that currently carry out these activities independently;

- where force majeure clauses in commercial contracts might be triggered and lead either to a suspension of performance or trigger payments and/or the ability to terminate; and
- in the context of export control review - as the list of products that are potentially dual-use can be extremely wide.

Gide's International Trade & Regulation Team in Brussels and London will provide further updates and guidance as matters continue to unfold.

Our Team will gladly assist you should you have questions or need legal assistance in ensuring compliance when dealing under the newly adopted sanctions.

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