Client Alert

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Broad, Sweeping Economic Sanctions a Certainty upon a Russian Invasion of Ukraine

American exporters likely to be affected in multiple material ways

President Joe Biden made it abundantly clear earlier this week that any Russian invasion of Ukraine would trigger an American and European response of the most immediate, targeted and most punitive sanctions the world has ever seen. Such measures are currently being drafted in response to the Russian military buildup at Ukraine's border.

In the past, the U.S. response to significant international transgressions has been the implementation of slow, gradual and escalating sanctions against the perceived violating country, company or individual. Such was the case in 2014, in the first Russian invasion of Crimea. Those limited sanctions, gradually imposed on Russia, took years to fully implement and remain in effect today. However, the breadth, depth and expanse of the sanctions that will be implemented upon a full-scale Russian invasion of Ukraine are anticipated to be quite different. The current likely response will be immediate, targeted, severe and punitive. And, they will no doubt have a significant impact on U.S. businesses. As President Biden himself acknowledged, "liberty does not come without cost." He further stated on February 15 that, "I will not pretend this will be painless." The "cost" and "pain" that the President is talking about is economic pain to American business in the form of trade restrictions on U.S. businesses, and to individuals in the form of higher prices at the pump, in addition to other consequences.

Anytime a country as powerful as Russia is the target of such a sanction regime, the consequences are hard to fully imagine. Nevertheless, some aspects of a sanctions regime are clear. It appears that the Administration has learned from past failures, and will target Russia's most immediate vulnerabilities: its banking and financial systems and processes; its oil and gas business which constitutes two-thirds of the country's revenues; and finally its technology industries.

President Biden stated on February 17 that, "If Russia proceeds, we will rally the world and oppose its aggression." The President explained: "The

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United States and our allies and partners around the world are ready to impose powerful sanctions and export control." Unlike typical laws, export controls and sanctions can be imposed solely on the issuance of a President's unilateral executive order. Under the International Economic Emergency Powers Act (IEPPA) and the Export Administration Act (EAA), the President has the authority with the stroke of a pen to issue executive orders that require the other departments in the Executive Branch, Treasury, State and Commerce, to issue regulations bringing the Executive Order's aims to fruition. No vote in Congress is needed.

These regulations are already in draft. These sanctions will include restrictions on Russian banks that would dramatically affect Russia's ability to conduct international business. Russia would be eliminated from the "SWIFT" banking system, thereby denying it access to international finance and capital. Russia would only be able to conduct unilateral trade with individual trading partners. Russia has long been attempting to create its own system to replace SWIFT. However, currently, only 12 financial institutions subscribe to this fledgling proposed alternative, including one Chinese bank. It is far from a substitute for SWIFT currently.

Russia is a major exporter of rare-earth minerals and metals – such as titanium – which is used in automotives and airplanes. Russia supplies about one-third of the world's palladium, a rare metal with many industrial applications. As such, U.S. officials have warned of supply disruptions in the semiconductor and aerospace industries as sanctions will directly affect these businesses. A senior U.S. administration official stated this week that the United States is working with its European allies and partners to ban exports of technology and products used in artificial intelligence, quantum computing and aerospace. No doubt then, that sales of these minerals, rare earths, <u>and all other products that support these industries</u>, to Russia and Russian businesses will be banned. The export controls would come in addition to more traditional economic and banking sanctions that would hurt the Russian economy. The "novel" sanctions are intended to cripple Vladimir Putin's ambition in key sectors, beyond just oil and gas, as he tries to diversify the Russian economy.

The idea of sanctions is to hurt the target more than you harm yourself. However, there is no doubt that there will be collateral consequences to U.S. businesses. This is the "pain" that the President is referencing. Well, how will U.S. businesses be hurt? We need only look to the recent sanctions against the Chinese military apparatus that went into effect on June 21, 2021. In these recent Chinese sanctions, currently any sale and export of any item that supports the Chinese industrial complex requires a license application. Most will be denied. This sanction affects thousands of businesses in this country, as the Chinese "military apparatus" includes thousands and thousands of Chinese companies, universities, organizations and individuals. Selling a paperclip to one of these entities now requires a

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White Collar Defense & Government Investigations license. A sale and export without an export license from the Commerce Department results in a violation that could come with severe penalties such as heavy fines, imprisonment, in the case of knowing and intentional violations, and possible debarment – losing export privileges.

Applying a similar approach to Russia, it is likely that the Russian military, technological, and energy apparatuses may be the subject of similar, broad sanctions. If this is the case, any U.S. business that sells, directly or indirectly, any U.S. product to any company, organization, university or individual that is part of these industries, will be ensnared.

The United States and its European allies are preparing contingency plans in the event Russia cuts off energy exports to Europe. Already, the Administration has been working to identify suppliers in North Africa, the Middle East and Asia that could provide a temporary stop gap to Europe. However, there is no doubt that energy costs will rise substantially because of disruptions. The question is, who will blink first? Russia is sitting on $630 billion in cash reserves, and Putin may think he can ride out any sanctions the West could impose.

The world is likely to see the most massive trade restrictions imposed in the quickest time in history if Russia invades Ukraine. And along with it, the most devastating consequences to global trade. U.S. businesses that provide any tangential support to Russian companies or industries, or have any connection to the Russian financial or banking systems, should prepare to navigate likely sanctions immediately.

Please contact the Olshan attorney with whom you regularly work or the attorney listed below if you would like to discuss further or have questions.

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