Sanctions against Russia over Ukraine

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- A significant and expanding sanctions regime against Russia has been in place since March 2014
- The downing of the Malaysian Airlines flight increased tensions
- The EU announced broad economic sanctions against Russia on 29 July 2014 including restrictions on some state-controlled Russian banks' ability to borrow money in EU financial markets and an arms embargo
- A ban on the export of technology to do with the extraction of oil from deep sea, Arctic and shale deposits was also announced
- The US increased the range of its sanctions on the same day
- Reaction in the UK press has been mixed

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1 Sanctions regime set up in March 2014

1.1 EU sanctions

Council Decision 2014/145/CFSP[1] and Council Regulation (EU) 269/2014,[2] of 17 March 2014, imposed visa bans and asset freezes on certain individuals associated with 'actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine'.

There are two separate instruments because the action affects matters covered by both the Common Foreign and Security Policy (CFSP) and the Treaty on the Functioning of the EU (TFEU).

The European Scrutiny Committee considered the implementing decisions for the sanctions on 30 April.[3] The Committee cleared the documents, decided that they were politically important and requested further information from the UK government.[4] Further information about the measures is available in the Committee's report.

More names were added on 29 April and the list has been amended since then.

The sanctions were broadly in line with the US restrictions, and other countries such as Japan and Australia have adopted similar measures.[5] Russia retaliated by implementing some similar sanctions. On 7 May, the EU Council expanded the criteria to make it easier to add Russian companies to the list, thereby bringing the EU sanctions list more in line with that of the US government.

On Monday 23 June, the then British Foreign Secretary William Hague warned that the EU was prepared to impose more sanctions on Russia if necessary.[6] The EU has made refraining from imposing new sanctions conditional on the Russian reaction to the new Ukrainian government's peace plan.

A package of economic measures, which could damage both the Russian and the EU economies, has reportedly been drawn up by the EU. It is not clear how far they would go although it has been reported that they are divided into different stages of severity.

2 Options for further action

Some Ukrainians have expressed frustration that economic measures have not already been implemented. A Ukrainian NGO said on 14 June:

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1 Council Decision 2014/145/CFSP of 17 March 2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine

2 Council Regulation (EU) No 269/2014 of 17 March 2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine

3 European Scrutiny Committee, Documents considered by the Committee 20 April 2014, Ukraine and Russia: EU restrictive measures

4 European Scrutiny Committee, Documents considered by the Committee 20 April 2014, Ukraine and Russia: EU restrictive measures

5 Russia Sanctions developments, provided by the law firm Baker and McKenzie, provides some useful information

6 'Hague says EU ready for more Russia sanctions if necessary', *Reuters,* 23 June 2014

> It is very difficult to understand why we are still hearing threats that 'a failure by Russia to de-escalate this situation will lead to additional costs.' Russia has not just failed to de-escalate the situation. It is actively escalating it.[7]

However, the different EU member states have diverging economic interests in Ukraine. German companies are reported to be reluctant to hamper trade, the UK financial sector benefits from Russian money, and many Central and Eastern European countries are highly dependent on Russian gas and on Russian spare parts for the Soviet-era weaponry in their armed forces.

A Commission document written in April was leaked recently that listed some options for tougher sanctions. It divided possible action into three levels:

1.1 Low intensity action

This would involve the following restrictions:

- adding more individuals to the existing restrictions list and also some entities
- suspending grants and stopping loans from the European Investment Bank

These action have already been taken.

There were also proposed restrictions on:

- imports of Russian luxury goods (diamonds, precious metals, furs, vodka and caviar) and of food products;
- selected … intermediate and processed goods (fertilisers, chemicals, tyres, vessels" but not "steel or nuclear components";
- imports and exports of arms; and
- export financing for the listed industries.[8]

1.2 Medium intensity action

This would involve the following measures:

- a ban on imports of all intermediate and processed goods;
- a ban on imports/exports of "all sensitive technologies and dual use and arms";
- blacklisting still more Russian individuals;
- "restrictions" on "trade and investment and related financial services";
- restrictions on "free movement of capital";
- restrictions on "maritime and road transport (not air transport)";
- "holding up Russian investment/acquisition in the energy sector";
- "import ban on coal (no ban on electricity)"; and

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7 'Barroso agrees new Russia talks, as warfare escalates', *EUObserver,* 14 June 2014

8 'Leaked paper: EU options on 'stage three' Russia sanctions', *EUObserver,* 22 July 2014

- “cancellation of all co-operation activities”.[9]

1.3 High Intensity action

This would involve the following:

- “capital market restrictions”;
- “prohibition of new investment in Russia”;
- “strict application of EU regulatory rules to Russian assets in EU companies”;
- an “import ban on gas”; and
- “an import ban on oil”.[10]

It should be borne in mind that this is only a report of a leaked document and serves more as an indication of the range of options being discussed since the spring. In the event, discussions in the EU appear to have at the very least re-ordered the options.

3 US sanctions of 16 July

On 16 July, the US administration imposed restrictions on large Russian companies, including GazpromBank and Vnesheconom Bank and gas producer Novatek and the government-controlled oil company Rosneft. The restrictions prevent people in the US from providing funding for the companies, effectively restricting the companies’ access to US capital markets. Some Russian defence companies had their assets in the US frozen. The administration also added the names of four Russian officials to the existing sanctions list. More detail is provided in a US Treasury press notice:

- Treasury imposed sanctions that prohibit U.S. persons from providing new financing to two major Russian financial institutions (Gazprombank OAO and VEB) and two Russian energy firms (OAO Novatek and Rosneft), limiting their access to U.S. capital markets;
- Treasury designated eight Russian arms firms, which are responsible for the production of a range of materiel that includes small arms, mortar shells, and tanks;
- Treasury designated the “Luhansk People’s Republic” and the “Donetsk People’s Republic,” which have asserted governmental authority over parts of Ukraine without the authorization of the Government of Ukraine; and Aleksandr Borodai, the self-declared “prime minister” of the Donetsk People’s Republic, for threatening the peace, security, stability, sovereignty, and territorial integrity of Ukraine;
- Treasury designated Feodosiya Enterprises, a key shipping facility in the Crimean peninsula, because it is complicit in the misappropriation of state assets of Ukraine; and
- Treasury designated four Russian government officials, including Sergey Beseda, a senior Russian Federal Security Service official.[11]

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9 ‘Leaked paper: EU options on 'stage three' Russia sanctions’, *EUObserver,* 22 July 2014

10 *Ibid*

11 Announcement of Treasury Sanctions on Entities Within the Financial Services and Energy Sectors of Russia, Against Arms or Related Materiel Entities, and those Undermining Ukraine's Sovereignty, US Treasury press release, 16 July 2014

The Russian deputy foreign minister said that Russia would take 'acutely painful' measures in response.[12]

4 EU action 16 July

EU leaders at the European Council meeting of 16 July. The EU Council said that Russia had not sufficiently implemented the steps set out in their conclusions of 27 June, in which they had called on Russia to use its influence on the rebel groups and to stop the flow of militants and weaponry cross the border and to achieve rapid results in de-escalating the conflict.

The EU leaders stopped the European Investment Bank and the European Bank for Reconstruction and Development from granting further loans in the Russian Federation and instructed the European Commission to prepare a list of entities supporting the unrest by the end of July. Asset freezes and travel bans had already been placed on 11 new individuals on 11 July.

They also agreed to discontinue the suspension of licences for export to Ukraine of equipment that might be used for internal repression.[13]

The Council also asked the Commission to review EU bilateral and regional cooperation programmes with a view to suspending most of them. This would amount to some €450 million in aid being cancelled. Civil society programmes would be maintained.[14]

The Russian ministry of foreign affairs responded with disappointment to the EU sanctions:

> We are disappointed that the European Union, contrary to its own interests, has yielded to the blackmail of the US Administration and followed the path of sanctions against Russia. Brussels is actually copying the example of Washington, basically applying "mirror logic" putting full blame on those who take real efforts to deescalate the situation in Ukraine, while glaring facts including unceasing flow of refugees from Ukraine to Russia, shelling of Russian territory and other anti-Russian provocations are being blatantly suppressed.[15]

5 EU agrees further action following the MH17 disaster

The EU has ramped up its efforts to dissuade Russia from destabilising Ukraine partly because Germany has taken a stronger line. However, 'stage three' sanctions: restrictions against whole sectors of the Russian economy, have not been imposed yet, even though certain EU leaders, from the Baltic States and Sweden for example, think they are necessary. Dalia Grybauskaite, Lithuania president, said that without a tougher line, 'Russia will go on behaving aggressively on the borders of Europe'.[16]

After the MH17 Malaysian Airlines airliner crash on 17 July, the pressure grew for more action.

The UK Foreign Secretary, Philip Hammond, suggested that asset freezes and travel bans could be imposed on close associates of Russian leader Vladimir Putin. Press reports

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12 'EU targets Russian oligarchs, as US hits banks and oil firms', *EUObserver,* 17 July 2014

13 Special meeting of the European Council (16 July 2014) – Conclusions, European Council, 16 July 2014

14 European Council meeting 26/27 June 2014 – Conclusions, European Council, 27 June 2014

15 'Comment on European Council conclusions regarding the situation in Ukraine', Russian mission to the EU press release, 17 July 2014

16 'Germany backs more EU sanctions on Russia', *EUObserver,* 16 July 2014

suggested that the UK would be pressing for 'tier three' sanctions: targeting whole sectors of the Russian economy and imposing arms trade bans. David Cameron implicitly criticised those who might simply hope that the crisis would go away:

> For too long there has been a reluctance on the part of too many European countries to face up to the implications of what is happening in eastern Ukraine.
>
> Sitting around the European Council table on Wednesday evening I saw that reluctance at work again.
>
> Some countries, with Britain at the forefront, have consistently pushed for action that reflects the magnitude of the long-term threat. They tend to be the countries with the closest physical proximity to Russia and the most direct experience of what is at stake. Their own independence and nationhood have come at a high price. They never forget it. But others seem more anxious to make this a problem to be managed and contained, not a challenge to be met and mastered.[17]

22 July meeting

On 22 July, EU foreign ministers met to discuss Ukraine in Brussels. After the meeting, Frans Timmermans, Dutch foreign minister, said that 'forceful' and 'unanimous' decisions had been taken to widen the sanctions.[18] The existing sanctions process, agreed 16 July, would be accelerated, with a new list of names and organisations would be drafted by Thursday 24 July for addition to the sanctions list.

The press release on the meeting went on:

> The Council also requested the Commission and the European External Action Service to finalise preparatory work on possible targeted measures and to present proposals for action, including on access to capital markets, defence, dual use goods and sensitive technologies, including in the energy sector.[19]

The results of this work would be presented on 24 July.

24 July meeting

EU member states' ambassadors met in Coreper (the Committee of Permanent Representatives to the EU) on 24 July to consider further action. They added 15 more individuals, nine companies and nine institutions from Russia and east Ukraine to an existing list of 72 individuals and two firms. They also agreed to change the criteria for adding names to the list to allow people close to the Russian president to be added. Discussions continued on 25 July, reportedly to consider broader trade and financial sanctions.[20] The sanctions would restrict access by Russian companies and banks to European capital markets.

25 July meeting

The Committee of Permanent Representatives (Coreper), member state ambassadors to the EU, met on Friday 25 July. They adopted the measures agreed at the Foreign Affairs Council of 22 July. The legal acts passed make it possible:

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17 'MH17 air disaster: article by David Cameron' Downing Street press release, 20 July 2014
18 'MH17 plane crash: EU to widen Russia sanctions', *BBC News Online*, 22 July 2014
19 'Foreign Affairs Council meeting', EU press release, 22 July 2014
20 'EU blacklists more Russians, prepares economic sanctions', *EUObserver*, *24 July 2014*

- to target **15 additional persons and 18 new entities** with a travel ban and assets freeze. In total, therefore, **87 persons and 20 entities** will now be under EU sanctions over the situation in Ukraine
- to **extend the designation criteria** for imposing asset freezes and visa bans on **persons and entities that actively support or are benefiting from the Russian decision-makers** responsible for the annexation of Crimea or the destabilisation of Eastern Ukraine.[21]

Some of the individuals added to the list were members of Russia's Security Council. Others were rebel leaders in Ukraine.

The meeting also discussed the work on broader economic sanctions, including access to capital markets, defence, dual use goods, and sensitive technologies, including in the energy sector.

On 25 July the Council duly adopted the proposals from the Coreper meeting the previous day. These became law with publication in the Official Journal on 25 July.[22] The decision was adopted by written procedure, a special procedure for urgent measures.[23]

6 Economic sanctions announced in EU, additions in the US

The broader economic sanctions discussed at Coreper are widely referred to as 'tier three' sanctions and have been described as the hardest since the Cold War. The arms embargo only applies to future contracts, as do capital market restrictions and oil technology export restrictions. This will allow the French government to go ahead with its sale of helicopter carriers and will also soften the potential blow of financial market restrictions to the City of London.

President of the European Council Herman Van Rompuy said that the proposed measures would be effective but not damage the European economy too much. He said the package:

> …strikes the right balance when it comes to cost/benefit ratio and scalability/reversibility over time. It should have a strong impact on Russia's economy while keeping a moderate effect on EU economies.[24]

In a conference call on 28 July, leaders of Britain, France, Germany, Italy and the US agreed to go ahead with EU trade sanctions. These will, like US sanctions already in place, impose restrictions on Russian banks' access to Western finance, in this case European and, particularly, UK financial markets. The legislation imposed:

- Restrictions meaning that 'EU nationals and companies may no more buy or sell new bonds, equity or similar financial instruments with a maturity exceeding 90 days, issued by major state-owned Russian banks, development banks, their subsidiaries and those acting on their behalf. Services related to the issuing of such financial instruments, e.g. brokering, are also prohibited.'[25]

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21 'Further EU sanctions over situation in Eastern Ukraine', Council of the European Union release, 25 July 2014

22 Council Implementing Regulation (EU) 810/2014 of 25 July 2014 implementing Regulation (EU) 269/2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine

23 'EU sanctions over situation in Eastern Ukraine strengthened', Council of the European Union press release, 25 July 2014

24 'EU to hit Russia with economic sanctions next week', *Euobserver,* 25 July 2014

25 'EU restrictive measures in view of the situation in Eastern Ukraine and the illegal annexation of Crimea', European Council background note, 29 July 2014

The listed financial institutions are:

1. Sberbank
2. VTB Bank
3. Gazprombank
4. Vnesheconombank (VEB)
5. Rosselkhozbank

- An embargo on the export and import of arms and related material, covering all items from the EU common military list.[26]

- An export ban on dual-use goods and technology for military end users, as defined by the EU list of dual use goods.[27]

- Restrictions on the export of technology connected with the deep water, Arctic or shale oil extraction, but not the gas industry.

Coreper met again on 29 July to finalise the sanctions and they came into force with publication in the Official Journal on 31 July,[28] using the written procedure.

The EU financial sanctions went further than the US measures in that Sberbank, Russia's biggest, is not listed by the US Treasury. On the other hand, the US Treasury designated the Bank of Moscow, while the EU did not.

6.1 Extra sanctions related to Crimea

The Coreper meeting of 28 July also agreed on specific trade and investment restrictions for Crimea and Sevastopol, as requested at the European Council of 16 July.

These comprise a ban on new investment in, and the export of equipment for, the following sectors in Crimea and Sevastopol:

- infrastructure projects in the transport, telecommunications and energy infrastructure

- oil, gas and minerals exploitation infrastructure

Finance and insurance services related to such transactions were also banned.[29]

6.2 More additions to the travel bans and asset freezes list

Coreper also added eight individuals and three entities to the list of those subject to an asset freezes and visa bans, bringing the number of persons and entities under EU restrictions to 95 persons and 23 entities.[30]

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26 Common military list of the European Union (adopted by the Council on 17 March 2014)

27 Council Regulation (EC) No 428/2009 of 5 May 2009 setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items

28 Council Regulation (EU) 833/2014 of 31 July 2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine

29 'EU restrictive measures in view of the situation in Eastern Ukraine and the illegal annexation of Crimea', European Council background note, 29 July 2014

30 *Ibid*

6.3 More US sanctions

The EU's announcement of 29 July was coordinated with the US administration. The US Treasury imposed measures on more financial institutions, prohibiting US citizens and persons within the United States from:

> …transacting in, providing financing for, or otherwise dealing in new debt of longer than 90 days maturity or new equity for Bank of Moscow, Russian Agricultural Bank [Rosselkhozbank in Russian], and VTB Bank OAO, their property, or their interests in property.[31]

VEB and Gazprombank had already been listed on 16 July.

The US Treasury also designated and blocked the assets of United Shipbuilding Corporation 'for operating in the arms or related materiel sector in Russia,' pursuant to Executive Order 13661 on persons contributing to the situation in Ukraine.[32]

7 Arms and dual-use licensing

7.1 UK strategic exports

Controversy broke out with the publication on 23 July 2014 of the House of Commons Committees on Arms Exports Control report on arms exports.[33] The committee reported that some arms exports to Russia were still being licenced, despite David Cameron's statement in the House of Commons that the UK had already said that it would not sell any more arms to Russia.[34] Paragraphs 472-4 of the Committees on Arms Export Control's report summarises what the Government had already done, giving a table of suspended licences.[35]

Responding to questions about apparent discrepancies prompted by the report and the Committees' chairman, Sir John Stanley MP, a government representative said:

> This government has never exported missiles or missile parts to the Russian military. The UK has granted an export licence for the Brazilian navy which enables their vessels to be repaired in 23 countries around the world, including Russia. This covers a wide range of equipment, including components for navy vessel missile launchers but these are exclusively for use by the Brazilian navy and not by Russian forces.

The statement continued:

> In March the former foreign secretary announced the suspension of all export licences to the Russian armed forces for any equipment that could be used against Ukraine. This report covers exports in 2013 before the suspension was in place. The majority of export licences that remain in place for Russia are for commercial use but we are keeping all licences under review. [..] We will not a grant a licence where there is a clear risk the equipment might be used for internal repression.[36]

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31 'Announcement of Additional Treasury Sanctions on Russian Financial Institutions and on a Defense Technology Entity', US Treasury press announcement, 29 July 2014. For the complete list, see US Treasury Office of Foreign Assets Control, Sectoral Sanctions Identifications List, July 29, 2014

32 Announcement of Additional Treasury Sanctions on Russian Financial Institutions and on a Defense Technology Entity', US Treasury press announcement, 29 July 2014

33 Committees on Arms Export Controls - First Report, *Scrutiny of Arms Exports and Arms Controls (2014),* HC 186 2014-15

34 HC Deb 21 July 2014, c1157

35 Committees on Arms Export Controls - First Report, *Scrutiny of Arms Exports and Arms Controls (2014),* HC 186 2014-15, para 472

36 'UK arms export licences for Russia still in place despite claims of embargo – report', *Guardian,* 23 July 2014

The UK's arms export regime is consistent with the EU-level regime.[37] Both regimes are legally binding. The operative document remains the Consolidated Criteria.[38] These criteria operate at both the national and EU-level and are the basis for all UK licensing decisions unless and until the EU agrees additional measures.

The value of UK military and dual-use sales to Russia is small. In 2012, the total value of licences issued was £48.5 million.[39] This compares with a total value of EU arms export licences issued in 2012 of £193 million but, unlike the UK figure, this does not include dual-use items so the two figures are not comparable.[40]

7.2 Russian imports

Russia is not a large arms importer from any other country either. Its only really large order in recent years is for the French Mistral helicopter assault ships. According to the *Financial Times,* Russia has only signed 10 significant defence import contracts since 2000:

- 4 light transport aircraft from the **Czech Republic**;
- diesel engines from **Germany**;
- 8 drones from **Israel**;
- 60 light armoured vehicles from **Italy**;
- 2 Mistrals from **France;**
- light helicopters and 4 amphibious landing craft to complement the Mistrals; and
- from **Ukraine**, 264 engines,
- 34 transport aircraft and
- 100 guided missiles.[41]

Most other orders are for small and technologically simple items, acceptable versions of which could probably be produced domestically.

7.3 Mistral French helicopter assault ships

The Mistral class is a helicopter carrier, capable of carrying 16 helicopters, up to four landing craft, 60 armoured fighting vehicles and 450 troops.[42] With a value of about $600 million each, the Mistrals are an important part of Russia's plans to modernise its military and make it more flexible and adaptable.

French president François Hollande says that the first of the two Mistral amphibious assault ships will be delivered in October but that the second delivery will depend on Russia's actions in relation to Ukraine. On 21 July, David Cameron criticised the proposed delivery: 'in

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[37] For information on how the UK's arms export control regime works, see *UK Arms Export Control Policy* - Commons Library Standard Note, 24 April 2014

[38] The full text of the Consolidated Criteria is at the end of the Standard Note cited above, in footnote 32

[39] Strategic Export Controls Annual Report Data for 2012. NB: the 2013 Annual Report Data gives a figure of £122.6 million

[40] EU Arms Export Controls Report 2012

[41] 'Russia has little to lose from arms embargo', *Financial Times,* 22 July 2014

[42] *The Military Balance 2014*, International Institute for Strategic Studies, p96

this country it would be unthinkable to fulfil an order like the one outstanding that the French have…'[43] Hollande said on the same day: 'For the time being, a level of sanctions has not been decided on that would prevent this delivery.'[44] A spokesperson for the President said: For now, France wants the sanctions to be financial, targeted and quick'.[45]

8 Economic costs for the EU

EU member states have varying economic interests and that has made forming a united front difficult. With the weak overall economic picture in the EU, one commentator expressed concern that the crisis between Russia and the West could tip the Eurozone into deflation.[46]

Uncertainty
The uncertainty created by a gradually growing sanctions regime could be one of the biggest effects of the present situation. Indeed it may be that the EU is happy with a step-by-step approach, because the uncertainty this causes may itself have a more serious effect on the Russian economy than in the West.

A Commission paper seen by journalists mentions uncertainty and capital flight:

> Restricting access to capital markets for Russian state-owned financial institutions would increase their cost of raising funds and constrain their ability to finance the Russian economy, unless the Russian public authorities provide them with substitute financing. It would also foster a climate of market uncertainty that is likely to affect the business environment in Russia and accelerate capital outflows.[47]

Retaliation
Russia is likely to take retaliatory measures. A group of members of the Duma has proposed banning the big Western auditing firms from Russia. Deloitte, KPMG, Ernst and Young, PriceWaterhouseCoopers, Boston Consulting Group and McKinsey are mentioned in press reports. Another bill is being drafted to provide for the confiscation of Western assets in Russia.[48] Neither bill is certain of being passed into law.

BP
The British oil company BP has a 20% stake in Rosneft, the state-controlled oil company that has already been targeted by US financial sanctions.

On 29 July, BP released a second quarter results statement, showing that the Rosneft stake had boosted its earnings. However, it warned that further sanctions could damage the business:

> Any future erosion of our relationship with Rosneft, or the impact of further economic sanctions, could adversely impact our business and strategic objectives in Russia, the level of our income, production and reserves, our investment in Rosneft and our reputation.[49]

The City

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[43] HC Deb 21 July 2014, c1157
[44] 'Hollande: Delivery of second Mistral warship depends on Russia's 'attitude'', *Euractiv, 22 July*
[45] *Ibid.*
[46] Wolfgang Münchau, 'Europe must impose financial sanctions on Russia', *Financial Times,* 21 July 2014
[47] 'EU blacklists more Russians, prepares economic sanctions', *Euobserver,* 24 July 2014
[48] 'Duma hits back with proposal to ban Big Four auditing firms', *Financial Times,* 30 July 2014
[49] 'BP sees profits rise but warns of Russia sanctions risk', *BBC News Online,* 29 July 2014

But it is the City of London where much attention is focussed, at least in Britain. The US authorities' imposition of an $8.9 billion fine on French bank BNP Paribas for breaking US sanctions has had a chilling effect on relations with Russia already, according to one City lawyer:

> The big institutions are on a state of alert. The fine on BNP Paribas totally changed the game; a penalty of that type means their tolerance for risk in the area of sanctions is phenomenally low. They will not be making any brave calls on Russia or Ukraine.[50]

The UK banking regulators have been in discussions with UK banks on the possible impact of further sanctions but their exposure to Russian businesses is reported to be relatively modest.[51]

France

France's sale of two Mistral helicopter assault ships is the most significant arms purchase by Russia from Europe and the French government has resisted calls from some quarters to cancel the sale. Otherwise, Russia's defence imports from the EU are limited.[52]

The French car manufacturer Renault said that its sales to Russia had already fallen by 8% this year. Renault and its partner Nissan control Russian Avtovaz, the makers of Lada cars.[53]

Germany

German exports to Russia have declined sharply in the first four months of 2014.[54]

8.1 Gas

It is the possibility of restrictions on the import of Russian gas that would be the most significant for the EU. Several EU member states are highly dependent on that energy source, as the table at Appendix 1 shows. Austria, Belgium, the Czech Republic, Finland, Greece, Hungary, Poland and Slovakia are the EU countries that import more than half of their total gas consumption from Russia.[55] So far the EU has gone out of its way to avoid targetting the gas trade.

The UK imports no gas by pipeline from Russia. However, prices in the UK would probably be affected by EU restrictions, indeed this may already be happening. On Thursday 24 July, wholesale prices moved up slightly, despite warm weather and plentiful supplies at present.[56]

8.2 Russian money in the UK

There has been discussion of rich Russians resident in London and other investments in the UK. However, information about this tends to be anecdotal, as it concerns private individuals. Some were urging financial sanctions on figures such as Roman Abramovich, Alisher Usmanov and Mihkail Fridman, all of whom are thought to be relatively close to Vladimir Putin. John Whittingdale MP, vice-chairman of the Conservative backbench 1922 Committee, said that Vladimir Putin's allies should not be immune from sanctions just

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50 'Osborne warns UK on financial impact of Russian sanctions', *Financial Times,* 21 July 2014

51 *Ibid.*

52 'Moscow has little to lose from defence crackdown', *Financial Times,* 23 June 2014

53 'Europe's companies braced for recoil', *Financial Times,* 30 July 2014

54 *Ibid*

55 In the case of Finland, the amount of gas imported by pipeline from Russia amounts to more than the total consumption. This means that some of the gas is re-exported or goes to increasing reserves

56 'UK GAS-Prices edge up on possible new EU sanctions against Russia', *Reuters,* 24 July 2014

because they live in London. 'Nor should we exempt people or companies who have business dealings in London,' Mr Whittingdale continued.[57]

Financial experts say that capital could flow out of London, both from the property market and from other investments. However, a banker was quoted as saying on 24 July that there was no evidence so far of this happening.[58]

According to a Commission document, Russian state-owned banks used EU capital markets for nearly half of their bond borrowings in 2013.[59] London would be particularly affected by any such restrictions.

TheCityUK, a representative organisation for London's financial sector, argued that any fianncial sanctions should be clear and multilateral in evidence to the House of Commons Treasury Select Committee in May 2014:

- sanctions should be carefully considered and, if the Government deems them necessary, they should be given clarity by the full force of law rather than being expressed as voluntary codes of conduct or foreign policy objectives

- sanctions should be multilateral and consistent, ensuring that the UK is not disadvantaged internationally

- sanctions should be targeted, smartly designed, thought through for all their implications and reviewed regularly in seeking to ensure that sanctions orders are complied with, business is operating heightened due diligence processes, screening contracts and individuals, and deploying additional methods of assessing the impact of various sanctions regimes on their operations.[60]

In its written evidence, TheCityUK highlighted the cost of compliance measures rather than the cost of lost business or investment.

One City banker has argued that financial sanctions would not be a 'huge deal', directly. It is the indirect damage of uncertainty in the eurozone that would be the problem:

> Financial sanctions would not, directly, be a huge deal.
>
> But Britain is right next door to a massive external market (the Eurozone), which is more closely tied to Ukrainian and Russian events. Sanctions would be intended to worsen Russia's economic position, which could quickly blow back to the UK. The MH17 crash could bring home just how close the conflict is to consumers across Europe.
>
> That could spread the economic impact beyond small wobbles in Germany. Russian President Vladimir Putin has the potential to seriously disrupt the Eurozone and UK economies over the coming days, weeks and months.[61]

A researcher for Open Europe countered that the possible damage to the City is being overstated:

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57 'Cameron under pressure to punish Russian oligarchs', *Times,* 24 July 2014

58 'Sanctions could mean capital flight from London', *Times*, 24 July 2014

59 'EU blacklists more Russians, prepares economic sanctions', *EUObserver*, 24 July 2014

60 House of Commons Select Committee on the Treasury, Inquiry into the cost effectiveness of economic and financial sanctions, Supplementary written evidence submitted by TheCityUK, 6 May 2014

61 Will financial sanctions on Russia significantly damage the City of London?', *City AM,* 25 July 2014

> A pernicious myth has developed that the City is flooded with Russian cash, and that the UK could try to weaken EU sanctions on Russia. But while the Russian presence may be highly visible, the actual stock of Russian international investments in London is £27bn - a sizable amount, but only 0.5 per cent of total European international assets in the City. It's true that the latest EU sanctions would focus on finance, and if implemented, they would have a disproportionate impact on the UK. Of the €16.4bn (£13bn) raised in the EU by Russian state-owned companies through IPOs between 2004 and 2012, all took place on the London Stock Exchange. However, the actual damage would be small - in the region of hundreds of millions - as only 1 per cent of exported services in these areas go to Russian firms. The real question is why, despite their tough talk, France and Germany, unlike the UK, are not following through with action.[62]

Questions have also been raised about donations to the Conservative Party from wealthy Russians. There was particular controversy about a donation in July 2014 of £160,000 from the wife of a former Russian government minister to the Conservative Party in exchange for a tennis match.[63]

9 Reaction

Labour leader Ed Miliband said that the EU should be moving more purposefully towards imposing more sanctions:

> The heads of government of Europe should be meeting, they shouldn't just be leaving it to the foreign ministers. We need to raise sanctions on Russia, on individual corporations that have been part of what happened around the big decisions that have been made.[64]

The reaction in the UK press to proposed trade sanctions has been mixed, however. In a leading article, the *Daily Telegraph* said that they would hurt the UK while allowing other EU countries to continue with business as usual:

> …as we have observed before, this exercise seems largely designed to damage the City of London, while enabling other EU countries to carry on with the essentials of their relationship with Moscow largely intact. The deal under which France is building two warships for Russia will go ahead, for instance; and while existing financial contracts are to be honoured, London's institutions will inevitably take a bigger hit than anywhere else.
>
> What is the point of this? The haphazard set of restrictions imposed on 90 or so wealthy individuals and 20 institutions allegedly connected to Vladimir Putin's government is making no difference at all. Moreover, these sanctions are not even aimed at the administration itself, and it is questionable how much influence the oligarchs have over its decisions.[65]

The *Independent on Sunday* cast doubt on the EU's ability to follow through on its pronouncements with an effective foreign policy:

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62 'Will financial sanctions on Russia significantly damage the City of London?', *City AM,* 25 July 2014

63 'David Cameron to play tennis with Russian donor', *Financial Times,* 24 July 2014

64 Ed Miliband on BBC Andrew Marr Show, 27 July 2014, quoted in 'Ed Miliband attacks David Cameron over Russian oligarch donations', *Financial Times,* 28 July 2014

65 'Grandstanding over MH17 punishes us more than Putin', *Daily Telegraph,* 29 July 2014

> This incoherence may have led to the worst of both worlds. It means that the EU has struck a high moral tone while being unwilling to follow it through. We thus appear to be both weak and hypocritical.[66]

The newspaper called for the EU to see the situation through Russian eyes:

> For all our horror at the downing of MH17, the policy of the EU and its allies ought to be one of understanding Russian pride and of giving Mr Putin the space to pull back with dignity from a Ukrainian civil war in which he has nothing to gain.

Anthony Brenton, former UK ambassador in Moscow, argued that sanctions would be counter-productive, both because Vladimir Putin is riding high on nationalistic approval in Russia, and because it could force Russia to turn away from the West:

> Sanctions have the attraction of being visible and punitive. But they won't work. They bring to mind the Russian story of the peasant who, infuriated by the slowness of his horse, beats the poor beast to death, and thus has no means of transport, however slow. The West has deployed sanctions against Russia/USSR six times since the Second World War. They have never worked. The shambolic boycott of the 1980 Moscow Olympics - imposed as part of a range of sanctions following the invasion of Afghanistan - should give real pause to those now pressing for a boycott of Russia's 2018 World Cup. It was Afghan fighters, not Western pressure, that finally drove Moscow's soldiers out.
>
> In countries as prickly as Russia, sanctions simply strengthen the forces most hostile to the West. It has even become a badge of patriotic pride among senior Russians to be on the sanctions list. Every new round reinforces Putin's standing with the public as their champion against a predatory West. Sanctions also strengthen that significant body of elite Russian thought which argues that Russia's dependence on economic links with the West is dangerous. They want to see a much more autonomous and state-led style of development - to slam the door on the Western influence and ideas which have been one of the most hopeful developments in Russia's sad recent history. Given this, it is no surprise that even key political opponents of the Putin regime, notably Mikhael Khodorkovsky, have condemned sanctions as counterproductive.[67]

The *Guardian*, too, suggested that an acceptable political settlement in Ukraine was necessary and that sanctions could be counter-productive:

> Mr Putin faces long-term economic prospects that are not that good, as the balance in world energy supply shifts away from Russia because of the boom in American energy production. Why not, the hawks might argue, shove him harder against the wall than he already is? The answer is that, given his character and his perception that a malign west is trying to demote and isolate Russia, this might well produce, not a withdrawal from Ukraine, but an expansion of military meddling there. Sanctions should be calibrated in such a way as to make the Russian leader reconsider.
>
> They should also be accompanied by moves that could lead to a settlement in Ukraine he might find tolerable, or at least give him cover for a change of approach, as well as being acceptable to Kiev. The excesses of Russian policy have obscured the fact that there is a genuine issue about the future of those Russian speakers in Ukraine who did not welcome the Maidan revolution and remain hostile to Kiev. The Putin regime has certainly manipulated and magnified their grievances, and the separatist rebels effectively block communication between those in the east who would be ready to

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[66] 'Don't add to Putin's catastrophe', *Independent on Sunday,* 27 July 2014

[67] 'Sanctions won't work – we will have to negotiate with Vladimir Putin', *Daily Telegraph,* 24 July 2014

negotiate a devolution agreement and Ukrainian president Petro Poroshenko. But that does not alter the fact that it needs to be settled if there is to be peace in Ukraine. Mr Putin is trapped in his own contradictions here. He seems to have decided against an annexation of eastern Ukraine, yet maintains a presence there that makes sense only if that is his intention. An autonomy that satisfies most easterners and also tells those who would prefer to be part of Russia that they must rest content with that is his only realistic objective, unless he simply wants to undermine and destabilise his neighbour.[68]

On 30 January, the *Times* appeared to welcome the trade sanctions, and implicitly criticised BP's warning that they would affect earnings:

> With respect to BP, if sanctions did not have an effect on some businesses operating in Russia, then they would not be worth imposing. Furthermore, BP, like all multinational companies, benefits from a world in which there is order and where shooting down commercial airliners and organising insurgencies in the territory of neighbours are discouraged. The reputation that matters is not the one it seeks to gain with capricious autocrats.
>
> The lesson is one that European governments themselves need to learn. There will be no gain in the new, tougher strategy towards Russia without pain.[69]

The *Financial Times* said that the sanctions were inevitable and mark the beginning of a much more difficult phase in relations between Russia and the West:

> The potential for a showdown between the west and Russia over Ukraine was implicit in Moscow's post-Soviet conception of its neighbours to the west and south as states that are less than fully sovereign and belong to a Russian sphere of influence. But Russia under the late Boris Yeltsin did not go to war outside its borders.
>
> Mr Putin lured Georgia into a short war in 2008 and recognised the breakaway regions of Abkhazia and South Ossetia as independent states. Mr Putin annexed Crimea in March. Now it is Mr Putin who is fomenting the pro-Russian rebellion in eastern Ukraine. Western governments must apply the new sanctions and be on guard against any further Russian misconduct.[70]

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68 'Ukraine sanctions: Revenge should not be our aim', *Guardian,* 23 July 2014
69 'Europe acts at last', *Times*, 30 July 2014
70 'Closing a 25-year chapter with Russia', Financial Times, 30 July 2014

European pipeline natural gas imports 2013

Natural Gas: Trade movements 2013 by pipeline
Billion cubic metres

To	From: Netherlands	Norway	United Kingdom	Other Europe	Kazakhstan	Russian Federation	Turkmenistan	Other Former Soviet Union	Iran	Algeria	Libya	**Total imports**	Total consumption	Russian imports as % of total consumption
Austria	-	1.2	-	0.5	-	5.1	-	-	-	-	-	**6.8**	8.49	60.59%
Belgium	5.4	9.4	2.5	-	-	12.3	-	-	-	-	-	**29.6**	16.82	72.84%
Czech Republic	-	3.8	-	-	-	7.2	-	-	-	-	-	**11.0**	8.42	85.43%
Finland	-	-	-	-	-	3.5	-	-	-	-	-	**3.5**	2.84	123.21%
France	6.5	15.5	-	0.4	-	8.1	-	-	-	-	-	**30.5**	42.83	18.85%
Germany	22.4	33.5	-	†	-	39.8	-	-	-	-	-	**95.8**	83.65	47.62%
Greece	-	-		0.6	-	2.4	-	-	-	-	-	**3.0**	3.58	66.37%
Hungary	-	-	-	-	-	5.9	-	-	-	-	-	**5.9**	8.56	68.91%
Ireland	-	-	4.9	-	-	-	-	-	-	-	-	**4.9**	4.50	0.00%
Italy	8.6	1.1		0.3	-	24.9	-	-	-	11.4	5.2	**51.6**	64.23	38.78%
Netherlands	-	4.8	1.6	13.0	-	2.1	-	-	-	-	-	**21.5**	37.07	5.65%
Poland	-	-	-	1.8	-	9.6	-	-	-	-	-	**11.4**	16.68	57.76%
Slovakia	-	-	-	-	-	5.3	-	-	-	-	-	**5.3**	5.39	98.82%
Spain	-	2.7	-	1.3	-	-	-	-	-	11.4	-	**15.3**	28.97	0.00%
Turkey	-	-	-	-	-	26.2	-	3.3	8.7	-	-	**38.2**	45.64	57.33%
United Kingdom	9.5	29.1	-	3.3	-	-	-	-	-	-	-	**41.9**	73.11	0.00%
Other Europe	0.8	1.2	0.0	6.8	-	10.0	-	-	-	2.0	-	**20.7**		
Europe	53.2	102.4	8.9	28.1	-	162.4	-	3.3	8.7	24.8	5.2	**397.1**		
Belarus	-	-	-	-	-	18.1	-	-	-	-	-	**18.1**		
Russian Federation	-	-	-	-	11.5	-	9.9	6.4	-	-	-	**27.8**		
Ukraine	-	-	-	1.8	-	25.1	-	-	-	-	-	**26.9**		
Other Former Soviet Union	-	-	-	-	0.2	5.6	1.1	3.8	0.7	-	-	**11.4**		
Former Soviet Union	-	-	-	1.8	11.7	48.9	11.0	10.1	0.7	-	-	**84.2**		

Source: Includes data from Cedigaz, CISStat, FGE MENAgas service, IHS CERA, PIRA Energy Group.

Data compiled in the *BP Statistical Review of World Energy June 2014*

Top exporters to and importers from Russia

Russia's top 10 export markets, 2012

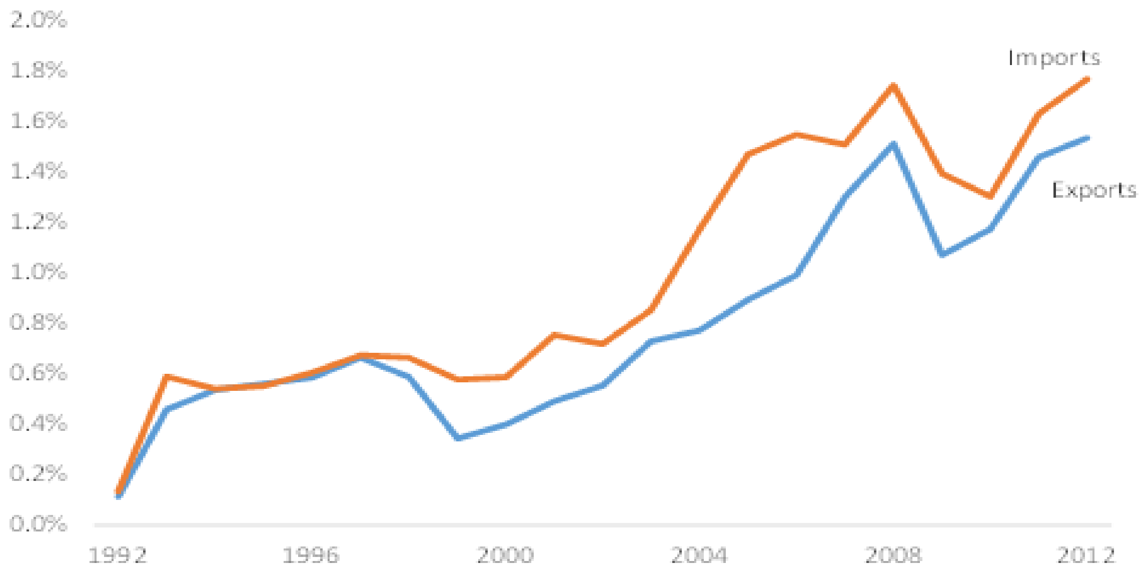
	Country	Exports from Russia, $bn
1	Netherlands	75.8
2	China	33.6
3	Italy	27.9
4	Germany	23.4
5	Belarus	20.8
6	Poland	19.6
7	Turkey	16.0
8	Japan	15.1
9	Ukraine	13.9
10	Republic of Korea	13.8
14	UK	9.1

Source: UNCTAD trade statistics

Russia imports of goods: top 10 sources

	Country	Imports, $ bn
1	China	49.7
2	Germany	43.8
3	Ukraine	19.0
4	Belarus	15.3
5	Italy	13.6
6	US	12.2
7	France	11.5
8	Japan	11.2
9	Republic of Korea	10.3
10	Poland	9.2
14	UK	6.9

Russia's share of UK exports and imports (Goods and services)



Source: UK Pink Book 2013, Table 9.3