



POLICY ALERT

ON IMPLEMENTATION OF INTERNATIONAL SANCTIONS BY GEORGIA

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INTRODUCTION

The Policy Alert raises questions for future consideration regarding the implementation of international sanctions and compatibility of domestic regulatory guidance.

The US Department of Treasury through its Office of Foreign Assets Control (OFAC), has imposed sanctions on two Georgian government officials and two private citizens for their roles in suppressing fundamental freedoms, including freedom of expression and peaceful assembly. According to the U.S. Treasury, these individuals were involved in violent crackdowns on protestors related to Georgia's controversial "foreign influence law," passed in May 2024. The sanctions, enacted under Executive Order 13818 as part of the Global Magnitsky Human Rights Accountability Act, specifically target those responsible for serious human rights abuses. Georgian banks should comply with the sanctions under the Magnitsky act, even if there is no dedicated domestic order for this.

The National Bank of Georgia (NBG), in its recent [September 2024] press statement, emphasizes that the country's financial sector adheres to international sanctions within its own regulatory framework.

NBG has issued numerous regulations and guidelines that require banks to comply with the sanctions. Order No. 208/04 issued in August 2023 was an additional layer introducing more legal clarity in the sanctions compliance framework specifically for sanctions against Russia and Belarus. The September 19, 2023 amendment to the above order introduced exceptions for Georgian citizens and legal entities owned by Georgian citizens, mandating banks to comply with the August order only in case of guilty verdict by the Georgian court. The September amendment introduces legal ambiguity, creates precedent, and sets a legal basis for replicating a similar approach in the case of other sanctions regimes. Notably, OFAC imposes sanctions unilaterally and immediately, without waiting for local judicial processes.

This ambiguous framework and regulatory and procedural incompatibility raises many important questions: What risks are associated with the adoption of NBG's relevant regulations? What consequences might third parties, financial institutions, and intermediaries face if they adhere to NBG rule? Could they incur penalties, operational restrictions, or reputational damage for facilitating transactions or maintaining business relationships with individuals targeted by international sanctions, such as those imposed by OFAC? What may be the potential implications for the general public and for the country more broadly?

IMPACT CHANNELS

US sanctions may have impact on Georgian banks through two main channels:

Secondary sanctions risk: if a Georgian bank engages with a sanctioned person(s) they risk getting sanctioned themselves for materially assisting sanctioned person.

Correspondent banking risk: international transactions in US\$ are primarily performed via US banks, which are required to comply with sanctions. If these correspondent banks, the number of which is very limited in case of Georgia, sense that doing business with Georgian banks is too risky, because they no longer comply with the sanctions, they may reconsider corresponding banking relationship. This will risk creating disruptions in international transactions and capital movement for Georgia's citizens and businesses.

POTENTIAL DISRUPTIONS

Despite the uncertainty in predicting future developments, it is important to consider the potential negative implications and economic disruptions associated with the risk of non-compliance with US sanctions:

Financial flow disruptions: Non-compliance can severely damage a company's reputation, leading to the loss of business and restricted access to the US financial system, which is essential for global banking operations. Reputational harm from sanctions violations can have long-lasting effects, often hindering a company's ability to maintain or rebuild trust with business partners and markets and secure access to capital markets. This damage goes beyond the banking institution, it can involve reputational damage for the country and its standing as an international partner.

Trade disruptions: OFAC's sanctions can lead to operational restrictions, including export bans, which can severely impact companies dependent on US technology or financial systems. Such actions can cripple business operations, particularly those that rely heavily on US resources or financial networks.

Remittances disruptions: The loss of corresponding banking relationships will significantly raise transaction costs for inward remittances, impacting the timeliness, affordability, and immediate access to these financial flows for Georgian citizens.

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