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INSIGHT

Russia Sanctions and Cryptocurrencies: Policy Issues

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The G-7 (Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States), the European Union (EU), and other countries have responded to Russia's expanded invasion of Ukraine in February 2022 with swift, coordinated, and broad sanctions designed to exert significant pressure on key Russian individuals and companies, as well as the broader Russian economy. As the multilateral coalition seeks to sustain economic pressure on Russia, and Russia seeks ways to mitigate the impact of sanctions, some in Congress are asking whether cryptocurrencies offer Russia a way to evade sanctions.

This Insight discusses related policy issues and proposed legislation; for technical analysis of cryptocurrency as a potential means of sanctions evasion, see CRS Insight IN11920, *Russian Sanctions and Cryptocurrency*, by Kristen E. Busch and Paul Tierno.

Are Transactions in Cryptocurrencies Subject to Sanctions?

The United States and G-7 partners have reiterated that sanctions apply to all transactions involving designated parties, regardless of the currency in which a transaction is denominated or the means used to complete a transaction. U.S. sanctions apply equally to transactions conducted in traditional fiat currencies (e.g., dollars, yen, euros, pounds, renminbi) and transactions conducted in cryptocurrencies or other digital currencies.

Is Russia Evading Sanctions with Cryptocurrency?

The pseudonymous nature of cryptocurrency may facilitate illicit finance by making payments more difficult to trace. However, the Department of the Treasury has found little evidence to date that Russian government officials or Russian individuals are using digital currencies to evade sanctions. Analysis by a private-sector blockchain analytics firm reached the same conclusion. More generally, the global cryptocurrency market is not liquid enough to backfill the financial needs of the entire Russian economy, the 11th largest in the world before the 2022 war. The collapse in the cryptocurrency market in May 2022 also highlights the volatility risk reliance on cryptocurrencies poses for would-be sanction evaders.

Reasons for concern remain. The cryptocurrency market is likely liquid enough to allow some Russian individuals and companies to transfer large sums of money. Actors associated with robust sanctions programs (most notably Iran and North Korea) have used cryptocurrencies to evade sanctions. At least one Russian legislator has suggested allowing friendly countries to pay for Russian oil and gas with cryptocurrency. New sanctions on Russia reportedly triggered suspicious activity in cryptocurrency markets. Trading between the ruble and Tether, a cryptocurrency, spiked after the G-7 announced a new round of Russia sanctions, and cryptocurrency exchanges in the United Arab Emirates (which has not imposed sanctions on Russia) have been deluged with requests from Russians to convert billions of dollars of cryptocurrencies. (Cryptocurrency exchanges are where cryptocurrencies can be exchanged for more-usable fiat currencies.)

More broadly, Russia has a track record of using digital currencies for illicit purposes. The Department of the Treasury characterizes Russia as "a haven for cybercriminals." In April 2022, the United States imposed sanctions on a Russian-based darknet market (Hydra) and virtual currency exchange (Garantex) that conducts most of its operations in Moscow for various illicit transactions.

The Department of the Treasury also has sought to limit the ability of Russian entities to raise funds through cryptocurrency mining (the creation of new cryptocurrency tokens). In April 2022, the Treasury designated companies and individuals operating in Russia's virtual currency mining industry as facilitators of sanctions evasion. Russia's crypto mining industry relies on imported computer equipment, and was estimated to be the third-largest bitcoin mining country in the world in August 2021.

Policy Options

Some Members of Congress have introduced legislation to prevent designated Russian entities from using cryptocurrencies as a sanctions evasion tool, such as S. 3867/H.R. 7429 and H.R. 7067. The bills would target foreign cryptocurrency entities processing transactions for sanctioned Russian entities and strengthen reporting requirements for international cryptocurrency transactions.

Secondary Sanctions on Foreign Cryptocurrency Firms

U.S. sanctions prohibit U.S. individuals and entities from transacting with sanctioned Russian entities; U.S. sanctions do not (and cannot) directly prohibit cryptocurrency firms in other countries from engaging in transactions with sanctioned Russian entities. Several major economies, including Brazil, China, India, Mexico, Saudi Arabia, and the United Arab Emirates, have not imposed sanctions on Russia, and sanctioned Russian entities could engage in fiat or cryptocurrency transactions with firms in these countries.

Proposed legislation would raise the costs for foreign cryptocurrency firms engaging in transactions with sanctioned Russian firms by imposing restrictions on any foreign cryptocurrency platform or "transaction facilitator" that assists or supports transactions with sanctioned Russian entities. These secondary sanctions could force foreign cryptocurrency entities to choose between (1) access to the U.S. financial system and U.S. dollar, and (2) transacting with sanctioned Russian entities.

Enhanced Reporting Requirements

Many cryptocurrency exchanges have adopted know-your-customer (KYC) anti-money laundering measures. KYC regulations help cryptocurrency exchanges enforce sanctions; for example, in March 2022, Coinbase, the largest U.S. cryptocurrency exchange, blocked 25,000 cryptocurrency wallets tied to Russians suspected of illicit activity. It is difficult to know how well all cryptocurrency firms apply KYC measures; further, the pseudonymous nature of cryptocurrency transactions complicates compliance with KYC regulations in place. Legislation could strengthen the effectiveness of KYC policy and support sanctions enforcement efforts by requiring U.S. persons to report on certain cryptocurrency transactions with financial accounts held outside the United States. However, the requirements would not pertain to non-U.S. persons and thus it is still feasible that Russians could use foreign exchanges to get around U.S. sanctions.

Cryptocurrency Industry Reactions

The cryptocurrency community in the United States is divided over the proposed legislation. Opponents argue that there is little evidence that wealthy Russians or Russian state entities are using cryptocurrencies to evade sanctions, and that legislation could undermine the privacy afforded to cryptocurrency users and stifle innovation in the industry. There are also general concerns that secondary sanctions could accelerate efforts by some actors to reduce their reliance on the U.S. financial system and the U.S. dollar.

Others argue that the legislation's effect would be minimal, because it would apply regulations to cryptocurrency transactions that the financial industry already applies to transactions using fiat currencies. Legislation could level the playing field for U.S. cryptocurrency firms by requiring all cryptocurrency firms to comply with U.S. sanctions (or risk losing access to the U.S. market and financial system).

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