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## The Sanctions Against Russia: What Did the West and the Media Expect?

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What does the conflict in Ukraine have to do with the Rotenberg brothers, Arkady and Boris? On the surface, not much, and yet these two businessmen from St. Petersburg are among the more than 100 individuals sanctioned by the US and the European Union in response to Russia's aggression against its neighboring country. They're not officials with a voice or a role in Russian policy or military action; nor are they part of the rickety power structure cobbled together by Russia in Crimea or Eastern Ukraine – categories which cover most of the people singled out for US and EU asset freezes and travel bans.

What distinguishes the Rotenberg brothers, Yuri Kovalchuk, Gennady Timchenko and a handful of others on the sanctions lists<sup>12</sup> is not what they did, but who they are – namely, long-time associates of Russian President Vladimir Putin, with ties that date back to his days as a city official in St. Petersburg, or his time as a KGB agent in what was then East Germany. Some share his KGB background, others, including the Rotenberg brothers, share his passion for judo, but all of them have become very rich, and some very powerful, during his 14 years in the Kremlin. They've profited from multi-million dollar state contracts in construction, oil, banking, and the media, or in some case, jobs at the top of multi-billion dollar state companies – perks that, in today's Russia, can only come with a blessing from the top.

But what is the point of targeting these particular men? They are hardly the only Russian oligarchs to get rich from sloppy state contracts generated by such mega-projects as the Sochi Olympics.<sup>3</sup> Yes, they are particularly close to the president but so too, in their day, was another band of oligarch-cronies – think Boris Berezovsky – who got rich and powerful in equally underhanded ways under another Russian leader, Putin's predecessor Boris Yeltsin. Are we suddenly shocked to find out that there is corruption and malfeasance at the top of the Russian government? So what are we setting out to do here – wage war on a kleptocracy, or get Russia to pull back from Ukraine? Is our goal to change Putin's policy, or change his regime?

Some experts argue that the sanctions targeting Putin's inner circle are tantamount to a political indictment of his regime. "The US government has

finally acknowledged publicly what successive administrations have known privately – that he [Putin] has built a system based on massive predation on a level not seen in Russia since the tsars,” writes Karen Dawisha, a professor at Miami University in the newly-released book *Putin’s Kleptocracy: Who Owns Russia*.<sup>4</sup>

Certainly, the decision to sanction Putin’s “cronies” grabbed headlines both in the West and in Russia – even though the most effective, and innovative, aspect of the Russian regime sanctions has to do with “micro-targeting,” which allows the US Treasury to zero in on specific Russian economic and financial activities, with minimum damage to US or Western interests.

When the story of the West’s sanctions against Russia is over, the headline will probably be about the efficiency of financial sanctions that block access by Russian banks and companies to Western credit markets. This is the latest implementation of an increasingly aggressive policy deployed after the 9/11 attacks, which has seen the US Treasury step up pressure on private banks, both American and foreign, to freeze the assets of targeted terrorist groups, drug lords, individuals and companies under US sanctions.

In the Russian case, the gradual closing of Western credit to Russian banks and companies has clearly magnified the country’s economic woes, brought about by a drop in oil prices and in the value of the ruble. It is difficult to untangle the precise impact of the sanctions in this gloomy picture, but even Putin has admitted that they are causing pain.

Still, it is the cronies, not the wonky financial measures, who were the first to capture public attention. By putting names and faces on the targets, the US and European Union governments – via the media – were able to give their domestic audiences, and critics, the impression that a gang of rich insiders who aided and abetted the Putin regime’s aggression in Ukraine, has been identified and targeted.

Maybe that was the point. Sanctions, after all, are to a large extent all about “the appearance of effective action.” As the late Richard Holbrooke said, they fill

the gap between “pounding your breast and indulging in empty rhetoric and going to war.”

But this approach has come under heavy criticism, particularly from experienced diplomats, who question the value of going after individuals – not because of their political roles, but because of their relationship with an elected leader. “I am very uneasy about this concept,” said Henry Kissinger recently. “What kind of international system do you have if every country goes around punishing individuals in other countries?”<sup>5</sup> Or, as a former CIA official said at a recent conference, “going after the leader of a country with which you have a big problem is not wise.”

Certainly, the ad hominem nature of these sanctions has not been lost on Moscow. “These sanctions are Obama’s private message to Putin,” said former central banker and finance ministry official Sergei Aleksashenko.<sup>6</sup> Putin himself referred darkly to US attempts at “outright blackmail.”<sup>7</sup>

Now, nine months later, the question of the effectiveness of the sanctions against Russia is coming due. Despite the evident damage to the Russian economy, there is little sign that the sanctions are compelling Putin to change course in Ukraine. If anything, he seems to have doubled down. One month after the July downing of the Malaysia Airlines flight in Ukraine that prompted the EU to toughen sanctions against Russia (including adding the names of Putin’s cronies), the Kremlin brazenly provided military assistance to the separatists in eastern Ukraine, reversing gains made on the ground by the Ukrainian army. Weeks after Putin helped draft a September cease-fire in Minsk, Russian personnel and hardware were again spotted moving into eastern Ukraine, a fact denied by the Kremlin even after it was captured on film.

Since then, as the sanctions hit home, Putin’s rhetoric has become, if anything, more belligerent as he continues to call on Russians to defend an embattled Russia. In a televised speech to the nation on December 4, 2014, he said the West has been attempting to encircle and weaken Russia for decades. The sanctions were nothing new, he said, and in his view, might have been imposed even if the Ukrainian conflict had not erupted. “If all that had not happened, they would

have come with a different mode to restrain Russia,” he said. “Whenever the West feels that Russia is becoming too strong, it resorts to such measures.”<sup>8</sup>

It is difficult to measure the impact of the EU and US asset freezes and travel bans against Putin’s cronies. Most of these men are adept at keeping their money hidden in offshore zones or moving it back to Russia, even selling off assets before they could be frozen. (Timchenko sold his shares in Gunvor that day after the US sanctions took effect.) In interviews, most of these men have scoffed at the sanctions, even as they regret not being able to visit children who are comfortably settled in the West.

Still, various indices show that Russia’s fabulously wealthy are feeling the pinch: of the 20 Russian billionaires on the Bloomberg Billionaires Index, 14 have lost money this year. As a group, they lost more than \$16 billion, or 7 percent of their total wealth.<sup>9</sup>

But if the purpose was to drive a wedge between the president and a powerful elite, that doesn’t seem to have happened. On the contrary, “The soldier’s task is to safeguard the commander, to get in front of the commander in the line of fire, to protect him with one’s chest, if need be,” said Vladimir Yakunin, the head of the state railways, and a longtime Putin friend who is on the US (but not the EU) sanctions list.<sup>10</sup>

“I think there is a perception that these oligarchs would pressure Putin but that’s got it wrong,” said Daniel Drezner, a professor at Tufts University, and expert on sanctions, in an interview. “I think the oligarchs need Putin a whole lot more than Putin needs them.”

If the goal was to expose the true nature of the Putin regime to the Russian public, there is some evidence that it is succeeding – thanks in part to what remains of an independent Russian media, but also, paradoxically, to the Russian government itself.

In October 2014, the Russian government, reversing its initial reluctance, came out in support of a draft law introduced in the Duma, or Russian parliament, by Putin’s party United Russia. The legislation would have taken money from the state budget to compensate individuals and companies affected

by the Western sanctions. It was quickly dubbed the “Rotenberg law,” since it was introduced shortly after Italy seized an estimated \$40 million in property – including a hotel in Rome and several villas in Sardinia – belonging to Arkady Rotenberg.<sup>11</sup>

“I have never heard of anything more cynical,” Boris Y. Nemtsov, a longtime critic of the Putin government in an interview with the New York Times.<sup>12</sup> Even Economy Minister Alexei Ulyukayev criticized it as an incentive for capital to flee Russia.

In the end, the proposed law barely passed its first reading on a remarkably close vote of 233 to 202; it was eventually withdrawn, felled by an unusual burst of outrage on the part of a usually docile opposition.

What is striking about the “Rotenberg law” was how quickly and openly it turned into an indictment of Putin’s self-serving clique. Nikolai Kolomeitsev, a Communist Party deputy, didn’t mince words in a speech before the Duma. “It turns out that the property rights of certain individuals, particularly those who are close [to power], are exceptionally more important than the property rights of millions,” he said.<sup>13</sup>

Certainly, the “Rotenberg law” reverberated among members of the Moscow elite who were surprised to watch the Russian government fall right into a trap of its own making. The blatant attempt to protect the president’s cronies at the public’s expense was widely reported by Russia’s independent media, particularly the business press which, in spite of government attempts to control information, continues to produce analytical reporting that is highly critical of the government’s economic policies.

“The loyalty of the elite is extremely important for the leader of a fortress under siege,” said an editorial in the Russian business daily *Vedomosti*. “With this law, the problem is solved: the national leader will buy the elite with the help of the budget.”

This kind of analysis has yet to seep through the propaganda blockade maintained by the state-controlled media, particularly television, which remains the dominant source of information for most Russians. But as times get tougher,

negative stories will get a more receptive audience. “In Russia, nothing the independent press does is futile,” said Leonid Bershidsky, a Berlin-based Bloomberg columnist, and former editor of several Russian business publications, in an email. “When people are unhappy, uncomfortable truths travel far, no matter how limited their initial distribution might be.”

### **The Media Outs the Oligarchs**

Inevitably, the media, both in the West and in Russia, had a key role to play in exposing the interlocking relationships between Putin and his very close and very rich friends. The US Treasury – which came out with sanctions against Putin’s cronies five months before the EU – set the stage in its press statements last March with the headline “Targeting Putin’s inner circle and certain related companies.”<sup>14</sup>

In citing Gennady Timchenko, for instance, the statement noted that he was a founder of Gunvor, one of the world’s largest commodities trading firms, “the funds of which may have been accessible to President Putin” – an unusually blunt accusation against a foreign leader. Yuri Kovalchuk was identified as “the personal banker for Putin and many senior officials, earning the moniker ‘Putin’s cashier.’” The allegations are striking but not conclusive: it wasn’t long ago that the slightly sinister moniker “Putin’s cashier” belonged to other oligarchs, Roman Abramovich and Sergei Pugachev, who are not on the sanctions list.

The same press statement cited the Rotenberg brothers’ “role in supporting Putin’s personal projects by receiving and executing high-price contracts for the Sochi Olympics,” which in the Russian context, does little to distinguish them from numerous other oligarchs, such as Vladimir Potanin, Oleg Deripaska and others involved in the Olympics project.

The Rotenberg empire goes well beyond Sochi. The two brothers, both long-time judo sparring partners of Putin’s at a gym in St. Petersburg, have economic interests in road building, energy projects and airport terminals. The elder brother, Arkady owns 51 percent of Stroygazmontazh Corporation, one of biggest contractors in the energy field; a 26 percent stake in Mostotrest, a big road

construction company; and 50 percent of TPS Avia, a construction firm that won a tender for a major passenger and cargo facility at Sheremetyevo airport near Moscow. The EU, which put Arkady (but not Boris Rotenberg) on its sanctions list in late July, cited his role in a proposed bridge linking the Russian city of Kerch and the Crimean peninsula.

In an article published in October 2014, *The New York Times* revealed an even more intriguing role for Arkady Rotenberg as chairman of a newly-privatized publishing company that now dominates the Russian text book market – after competitors were mysteriously eliminated by a complicit bureaucracy.<sup>15</sup> The textbook publishing house, which declared \$57 million in profits in 2013, is an insignificant addition to Rotenberg’s estimated \$3.1 billion portfolio, but it is clear that in Putin’s Russia, control of school books destined for the country’s 14 million schoolchildren is an important ideological asset.

These were the kind of details that came out in the Western media after that first round of sanctions, as news organizations rushed to answer the obvious questions: Who are these guys, and why are they being singled out? A sampling of headlines tells the story: “Putin’s Bank Trail Runs from Communist Cash to Russia’s New Billionaires,”<sup>16</sup> reads an April 16, 2014 headline in Bloomberg; “Comrade Capitalism: How Russia does Business in the Putin Era,”<sup>17</sup> was a multi-part series run by Reuters in May 2014; “Private Bank Fuels Fortune of Putin’s Inner Circle,”<sup>18</sup> was the lead article in a continuing series in *The New York Times*.

The stories mostly focus on a group of friends in St. Petersburg in the early 1990s where Putin, recently returned from East Germany, had taken a position as deputy to then-mayor Anatoli Sobchak. Back then, members of the group set up the so-called Ozero (Lake) Dacha Cooperative to manage a complex of cottages outside St. Petersburg. Several of them, in due course, became shareholders in Bank Rossiya, founded in 1990 with Communist Party money, which was to become the first Russian bank targeted by the US for, as the Treasury statement put it, “its close connections to Putin’s inner circle.” Shortly afterwards, Putin ordered the Russian Central Bank to help Bank Rossiya if needed, while state-

owned energy companies pumped up its capital by ostentatiously moving their accounts there.

In fact, much of the information about the now-notorious Bank Rossiya, and the Ozero Dacha Cooperative originated in the Russian press, which began investigating the intricate business relationships among Putin and his St. Petersburg friends in the early 2000s. *The New York Times* recognized as much in a prescient article, published in March 2012, entitled “The Midas Touch in St. Petersburg: Putin’s Friends Glow Brightly,” which profiled three members of Putin’s inner circle who were to be sanctioned two years later.<sup>19</sup>

“Legalities aside, these relationships are fixed in the public mind and widely reported by the Russian news media, so how Mr. Putin handles them could prove critical both to his near-term political survival and his legacy,” the reporters wrote.

In her book *Putin’s Kleptocracy*, Dawisha pays homage to the work of Russian journalists with an extensive bibliography that pulls together a wealth of their reporting, some of which has disappeared from the public record in Russia: she cites a 44-page article published in *Kommersant* in 2000, which was subsequently expunged from the paper’s archives.

Even now, in what remains of the independent media, investigative reporting continues, despite all apparent odds. Independent media such as the newspaper *Novaya Gazeta*, or the radio station Ekho Moskvi, business newspapers such as *Vedomosti*, and countless blogs and websites, have followed the story of Bank Rossiya and the Ozero cooperative. One example was *Novaya Gazeta*’s 2011 investigation of the Putin palace story that was at the heart of the 2014 Reuters investigation.<sup>20</sup>

The Western press has followed up with thorough investigations of the interlocking business relationships that link these men together. No one has been able to prove decisively to what extent Putin has personally profited from the phenomenal wealth accumulated by his friends, although rumors continue to circulate about tens of billions of dollars. The stories also document the intricate ways by which Russian businessmen pass state contracts through middle

companies, thus padding the bills and pocketing the difference. They have also tracked the money to offshore tax havens – in Cyprus and elsewhere – where several companies with unnamed owners or beneficiaries share the same mail box, allowing their owners to hide their profits.

These practices are hardly new in Russia: the chaotic privatization of the 1990s which created the fantastic wealth of the country's first generation of oligarchs involved similar schemes to siphon off profits, concealing them not only from Russian tax collectors, but also from unwitting partners, or shareholders.

In Yeltsin's day, the ruling elite were called "The Family," a sly, mafia-like shorthand for a group that included his top advisors, his daughter and her husband. Like the Putin gang, members of The Family shifted their money around the globe, through Switzerland, and more infamously, through the Bank of New York, snapping up villas in Europe, and sending their children to fancy Swiss and English boarding schools. The US Congress held hearings on the Bank of New York scandal, which resulted in the arrest of a highly-placed Kremlin official, while he was in New York.

These stories were closely followed at the time in the Russian media, which had grown very bold during the Yeltsin era, when it was possible not only to criticize, but to mock the Russian leader – now unthinkable. But the media in those years was also easily manipulated in what became an escalating war between dueling oligarchs – Vladimir Gusinsky and Boris Berezovsky – who didn't hesitate to use the freedom of the press to advance their interests and destroy their enemies. This background remains a cautionary note for researchers who rely on Russian press accounts.

Yet there is a distinction between Yeltsin-era oligarchs and their Putin-era successors. "In Yeltsin's time, an independent kleptocracy threatened to privatize the state," writes James Scherr in his book *Hard Diplomacy and Soft Coercion*. "Today a state kleptocracy distributes rent profit and property as it sees fit."

In her book, Dawisha argues that this kind of self-dealing is at the heart of the Putin regime's *raison d'être*: In her view, it was always Putin's goal "to create an authoritarian regime ruled by a close-knit cabal with embedded interests, plans

and capabilities.” The result, she writes, is “a Russia that is both a democratic failure and a resounding success – that is, a success for Putin and his cronies, and a success on his terms.”

The connections between Putin and his fast-rising St. Petersburg friends have long been an open secret in Moscow. In an interview with Bloomberg in 2007, Viktor Gerashchenko complained about the buddy system. “The problem arises when everything is oriented around one single man, with people around him who all grew up in the same courtyard,” he said. <sup>21</sup>

### **Sanctions: Are They Working?**

If the West has achieved one diplomatic victory with its policy of sanctions against Russia, it has been to maintain – not without difficulty – a unified stance within the transatlantic partnership. The most significant turning point was the downing of the Malaysian airliner over Ukraine which stiffened the EU’s resolve to hold Russia accountable, particularly in Germany, the key member in the alliance, and by far, Russia’s biggest European trading partner. Since then, German support for the sanctions against Russia has continued to rise, from 52 to 58 percent in a one-month period, according to a poll conducted for ZDF television in November 2014. <sup>22</sup>

In a tough speech made a day after she met with Putin at the G20 summit in Brisbane, Australia, German Chancellor Angela Merkel left no doubt about her determination. She warned Putin against “old thinking in terms of spheres of influences,” and vowed to keep up “economic sanctions against Russia as far and as long as they are necessary.”

Merkel’s speech would have dashed any lingering hopes in Moscow of driving a wedge between Washington and its European allies, a long-standing objective of Russian, and before that, Soviet diplomacy. All summer, and into the fall, Kremlin spokesmen kept telling European statesmen and audiences not to be pushed around by the Americans. At the Valdai conference in October, Sergei Ivanov, Russia’s first vice prime minister, reminded the Europeans in the

audience that the “economic sanctions demanded by Washington are hurting both Europe and Russia, but not the United States.”

As the pain inflicted by sanctions mounts, the state-controlled media has switched gears, moving away from the full-throated wartime propaganda of last summer. The tone now is more somber; articles appear about other historical periods when Russia was surrounded by “enemies.” The giddy euphoria over the “return” of Crimea has been replaced by appeals to the Russian people to brace for more sacrifice.<sup>23</sup>

This falls in line with Putin’s general theme that the country is under attack, particularly from America. The result, in the short term, is unlikely to be any softening of support for Putin, but rather the reverse. “The mentality of Russian society after the sanctions were enacted rather goes in the way of solidifying support for the Russian leadership than... lowering support for Putin and the policy he represents,” said Czech Prime Minister Bohuslav Sobotka.<sup>24</sup>

Most recent polls support this view, showing a majority of Russians insisting that the sanctions are having little impact on their lives, and that they may even be good for the economy by encouraging more local production, a point repeatedly made by Putin in public speeches. Oddly, the sanctions causing the most pain for ordinary Russians are the ones put into effect by Russia itself as a retaliatory measure, banning food imports from the EU, the US and other countries. The result has been a spike in grocery prices, a key factor in the sharp increase in inflation.<sup>25</sup>

### **How Sanctions Have Evolved**

From the start, the US and its European allies sought to avoid sanctions that would directly impact the Russian population. They also chose a strategy that allowed for a gradual escalation, which could be ratcheted up as Russia increased its interference, overt and covert, in Ukraine.

The days of broad trade embargos, such as the one the US had in place against Cuba for more than 50 years, or the sanctions against Saddam Hussein which had devastating consequences for the Iraqi people, are long over. In their place, the

West – with the US squarely in the lead – has developed targeted or “smart” sanctions which, piggy-backing on anti-money laundering laws and regulations, allow the US Treasury to compel private banks to steer clear of accounts held by targeted individuals, businesses or institutions. The aim is to squeeze elites, rather than average citizens, in an attempt to make governments change policy on everything from nuclear proliferation to support for terrorism to military aggression.

Drawing on the US Treasury’s unparalleled power over an international financial system that relies heavily on the dollar, this policy is able to “place the onus on banks to police their own system,” as Juan Zarate, a former US Treasury official describes in his book, *Treasury’s War: The Unleashing of a New Era of Financial Warfare*.

The new techniques were used first as a tool in the widening war against terrorism, but have since been deployed against nation states, such as North Korea, Iran and now Russia, and more recently the financial networks that support the Islamic State. At last count, there are 6,000 people on the US sanctions list. The US Treasury’s intelligence operation – the only such in-house operation of any finance ministry in the world – has grown from a staff of one person 13 years ago to one of 700 people today, with an annual budget of \$200 million, said David S. Cohen, the Treasury’s intelligence strategist and global enforcer, in a *New York Times* interview in October 2014.

Interestingly, the Treasury’s enforcement effort is increasingly dominated by military terminology. Zarate talks of having “weapons” that “reach beyond [US] shores to affect the bottom lines of our enemies.” Treasury Secretary Jacob J. Lew has boasted of opening up “a new battlefield for the United States.”

Many experts and diplomats agree that “smart” sanctions have been an effective diplomatic tool, for instance, in bringing Iran to the negotiating table over the future of its nuclear program. And many agree that the same sanctions have a key role to play in the international effort to force Putin to de-escalate in Ukraine. But many balk at the notion that economic coercion, in use since the

days of Sparta in ancient Greece, amounts to war, or that all targets – for instance, Iran or Russia – are necessarily “our enemies.”

The question is whether the new tactics of financial warfare – which are so tantalizingly effective in the short term – have come to dictate diplomatic strategy. Zarate argues that diplomats don’t understand the power of financial suasion. “It’s about diplomacy coming to terms with the nuance of these kinds of financial measures,” he said in an interview. “The whole idea of financial suasion has not been incorporated in our diplomacy.”

A US diplomat with long years of experience in Moscow takes a different view. “I start with the premise of the strategic objective we are after,” he said in an interview. “It is not clear whether we are trying to do an exercise in behavior modification, or are we out for regime change? What is the point of this all-out economic strategy, when the clear strategic purpose is not economic, but political? So far, it is hard to see the political impact of these sanctions.”

The reliance on “smart” sanctions is in itself proof of the unparalleled power of the US financial system. In 2014, the French bank PNB Paribas had to pay almost \$9 billion in fines for violating unilateral US sanctions against Cuba, Sudan and Iran, precisely because of its reliance on dollar clearing. “If you are a major European corporation, and you have US assets, or people with US passports, you need to follow US sanctions,” said Elizabeth Rosenberg, a sanctions expert at the Center for a New American Security, based in Washington, D.C.

Rosenberg said the Russian sanctions represent a “watershed moment” because they showed that financial sanctions can be narrowly targeted, and implemented gradually. “That makes it easier to get international consensus, and they can be ratcheted up as required,” she said in a telephone interview.

In March 2014, as the sanctions policy against Russia got underway after the Kremlin moved to annex Crimea, the US chose Putin’s friends as its first targets; the tougher so-called Level Three sanctions against Russia’s finance, energy and defense sectors came later, in stages. To some extent, that opening gambit was the financial equivalent of the pack of cards that identified the names and faces

of Saddam Hussein's associates as legitimate targets at the start of the 2003 Iraq war.

By targeting individuals close to the Russian president, the sanctions seemed to be making a statement not so much about Russia's policy in Ukraine, but about Putin himself and his regime. Kissinger in a recent talk at Harvard, traced it to the "demonization" of Putin, which in his view, has wrongly dominated US policy towards Russia. Other diplomats agree. "We have always bought the idea that Russia is run by one man; Josef Stalin is the default model," said a US diplomat with long experience in Moscow. "But saying it all comes down to one leader buries all kinds of other things."

Putin's own behavior – which can range from sulky to surly – has clearly tested the patience of his fellow world leaders, adding a personal element to the strong reactions to his policies in Ukraine. Merkel has reportedly been infuriated by his rude behavior and misleading statements; she was once quoted as saying that he "lives in another world." Obama has said Putin's "slouch" reminds him of the "bored kid at the back of the class."

But diplomats caution against an over-personalizing of the regime, which tends to obscure the dangerous risks at stake in the ongoing conflict over Ukraine. Thomas Graham, a senior fellow at Yale University's Jackson Institute and a managing director at Kissinger Associates, doesn't dispute that Putin has the last word in Russian foreign policy. "But we must remember that he operates in a political context," Graham wrote in an essay for the Carnegie Endowment for Peace. "He is a product of the Russian elite, and he gives voice to its consensus on Russia's role in the world." In short, Graham concluded, "we have a Russia problem, not a Putin problem."

Even if assuming that Putin is as all-powerful as many believe, there is little reason to believe that the targeting of his friends is going to change his behavior. Political scientists point out that in authoritarian regimes elites have to be convinced of an alternative leader's power to protect them before they get ready to switch sides. So far, no such alternative is apparent on the Russian horizon. "People in Putin's group have to accept enormous risks even to broach the subject

of change,” wrote Kimberly Martin, a Barnard College professor. “Who other than Putin could provide for their personal financial needs, while maintaining control of a vast country that faces huge demographic, economic and foreign policy challenges?”<sup>26</sup>

The geopolitical significance of Russia’s aggression in Ukraine, and its impact on East-West relations, overshadows the importance of outing his corrupt friends. Previous sanctions have targeted countries like Iran or North Korea that are on the margins of the world’s economy. That is not the case with Russia, which despite its myriad problems, ranked as the world’s fifth largest economy, in terms of purchasing power parity, and as eighth in terms of GDP in 2013. It has the world’s largest natural gas reserves, its territory takes up one sixth of the globe, and it carries the historical memory, and a dangerous history, of a once-great power.

In that context, some argue that it makes more sense to target sanctions so that the West can achieve what it wants, rather than pursue and punish unsavory characters. “A realistic and lasting solution would have to reflect the national interests and protect the dignity of both sides, including President Putin, yet most in Washington want to treat Putin as if he were Slobodan Milosevic, Saddam Hussein or Muammar Gaddafi,” wrote Robert Blackwill, a veteran US diplomat in an article in *National Interest*.

The ability of “smart” sanctions to reach their targets is acknowledged by most experts, although their impact is unclear, given the ability of sanctioned individuals to find ways to hide their assets, sometimes in plain sight. The names of real owners, or shareholders, can be shielded behind front companies registered in Cyprus and other offshore financial service centers. Until comprehensive international rules are in place requiring full disclosure of beneficial owners of companies and accounts, it is safe to assume that many of the targeted individuals have moved their money beyond the reach of even the US Treasury.

In October 2014, Arkady Rotenberg – together with a several major Russian companies, including the oil company Rosneft – filed a challenge against the EU

sanctions in the European Court of Justice's General Court. Such challenges have had a higher success rate in Europe than in the US, where targeted individuals have to go through an administrative process to get themselves taken off the list of Specially Designated Nationals administered by the Treasury's Office of Foreign Asset Controls.

In the US, individuals can be delisted if they can prove that they have stopped the activities that got them sanctioned in the first place. Only part of the original justification is publically available: most details are classified, and can be made available only by court order. "National security trumps a lot," said Erich Ferrari, a Washington lawyer who has handled many delisting cases. "From a legal point of view, a private citizen is not in a good position."

Most individuals who succeed in getting delisted from the OFAC registers are involved in criminal activities, such as drug dealing, which they are able to prove they have stopped. Those named under sanctions brought about by their government's policies have to first find out what activities put them on the list before they can stop them.

The friends of Putin, for example, represent a particular challenge, according to former Treasury official Zarate. "I don't see how they get themselves out of this without changing their nationality, or changing the regime," he said in an interview.

Zarate, now an advisor at the Center for Strategic and International Studies in Washington D.C., was one of the architects of the Treasury's policy of policing bad actors through the international finance system. In his book and in recent essays on sanctions, Zarate chafes at the reluctance of US diplomats to use the full force of the Treasury's new found arsenal. In an article for the *Financial Times*, he argued that the West should keep up the financial pressure on the Russian economy, and its elite, regardless of any diplomatic concessions.

"Sanctions should no longer be tied to diplomatic milestones," he wrote. "Instead they should be seen as a continuous campaign that leaves Mr. Putin and the market guessing." <sup>27</sup>

In an interview, Zarate argued that the sanctions against Russia have suffered from a lack of clear purpose, or narrative. “My criticism is that we have tied these sanctions to diplomatic markers which have not panned out,” he said. “That raises the question of who you are targeting and why. Is this targeting of those around Putin about Ukraine, or is it about their conduct?”

Of all the elements that go into the Western diplomatic response to Russia’s aggression in Ukraine, the targeting of Putin’s cronies seems the least promising, even though it may feel morally satisfying. “I am not super troubled by the sanctions against the buddies,” said one Western diplomat in an off-the-record interview. “Given the limitation on the tools we have to influence Russian behavior, applying sanctions against those who might have some influence doesn’t seem out of bounds.”

Whether the sanctions are about changing Putin’s policy, or about cleaning up Russia’s kleptocracy, it’s not clear how and when the West can start rolling them back – particularly if the Republican-controlled Congress moves ahead with plans to lock them into legislation. Many experts and diplomats, particularly in Europe, reject the option of relentless, open-ended economic pressure against Russia which they see as counter-productive, particularly at a time when the Russian economy has been plunged into crisis by a dramatic fall in oil prices.

The worsening of Russia’s economic situation in the closing weeks of 2014 has put the question of the original purpose of the sanctions in sharper focus. In December alone, Russia used more than \$11 billion from its foreign reserve funds to prop up the ruble, which last year lost almost 50 percent of its value as oil prices continued to fall, inflation rose and credit became ever scarcer.

At this critical juncture, the Western alliance now finds itself struggling to maintain its hard-won united front as the sanctions begin to have an impact on domestic economies as well as on Russia’s. In Europe, particularly in France and Germany, leaders have again offered Putin a way out. “I’m not for the policy of attaining goals by making things worse,” French President Francois Hollande said in an interview on France Inter Radio on January 5, 2015.

By opening the door to possible relief from sanctions, European leaders are reminding Moscow – and perhaps Washington – that their goal is not to cripple the Russian economy, or Putin’s regime, but to find a solution to the festering problem of Ukraine’s threatened sovereignty. In the US, this is often portrayed as a sign of weakness, a willingness to cave in to the pressure of business communities eager to resume trade with their giant neighbor.

But some argue that US interests are also at risk as a result of the unintended consequences of the sanctions. “Is it in the US’s interest to see massive capital flight out of Russia?” one top-level US diplomatic negotiator asked at a recent Harvard-sponsored conference on US-Russia relations. “Is it in the US’s interests to see Russia become a junior partner of China?” asked a top Russian expert.

If these were the goals of the West’s sanctions, then it is fair to say that they are working. It also may be that Putin’s cronies are feeling the pain. But so far, there is little sign that these results will succeed in forcing Russia to loosen its grip on Ukraine’s future.

## Endnotes

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