Tax Sanctions and the Russia-Ukraine Conflict

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I. Introduction

In January 2022, we wrote that the use of economic statecraft was at a high-water mark, with sanctions, tariffs, and export controls being used more than ever before.[1] Though that was true, it turned

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1 Ashley Deeks & Andrew Hayashi, *Tax Law as Foreign Policy*, 170 U. PA. L. REV. 275 (2021).

out that the waters have continued to rise dramatically in ways that we did not anticipate. The international economic response to Russia's most recent aggression in Ukraine has been unprecedented in its swiftness, severity, comprehensiveness, and creativity.[2] As one senior Biden Administration official put it in late January 2022, "[W]e are prepared to implement sanctions with massive consequences that were not considered in 2014. That means the gradualism of the past is out, and this time we'll start at the top of the escalation ladder and stay there."[3] Some commentators have described the initial rollout of sanctions as happening at "warp-speed," with the collection of economic measures taken against Russia representing a "sea change in sanctions practice globally."[4]

Starting at the top of the escalation ladder would seem to have one downside: there is nowhere to go but down.[5] And yet, as 2022 progressed and the war continued, a broad coalition of states found ways to escalate economic sanctions even further. Although the initial wave of sanctions had some effect on the Russian economy, leading to a brief devaluation of the ruble, the currency proved resilient as the Russian Central Bank doubled interest rates, imposed capital controls, and required exporters to convert some of their profits into rubles.[6] Perhaps most importantly, ongoing Russian oil

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2 Elena Chachko & J. Benton Heath, *A Watershed Moment for Sanctions? Russia, Ukraine, and the Economic Battlefield,* 116 AJIL UNBOUND 135, 135 (2022) ("Russia's invasion of Ukraine has triggered an unprecedented wave of sanctions targeting every facet of the Russian economy.").

3 White House, Background Press Call by Senior Administration Officials on Russia Ukraine Economic Deterrence Measures (Jan. 25, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/01/25/background-press-call-by-senior-administration-officials-on-russia-ukraine-economic-deterrence-measures/ [https://perma.cc/G57X-EDQ6].

4 Richard Oscar, *The War in Ukraine: A New Paradigm of Sanctions Practice*, LAWFARE (Aug. 22, 2022, 8:01 AM), https://www.lawfareblog.com/war-ukraine-new-paradigm-sanctions-practice [https://perma.cc/2XLS-7M8H]; Emily Kilcrease, Jason Bartlett & Mason Wong, *Sanctions by the Numbers: Economic Measures against Russia Following Its 2022 Invasion of Ukraine*, CTR. FOR A NEW AM. SEC. (June 16, 2022), https://www.cnas.org/publications/reports/sanctions-by-the-numbers-economic-measures-against-russia-following-its-2021-invasion-of-ukraine [https://perma.cc/P7SQ-LNYL] (noting that "the United States and its allies have issued a sweeping set of sanctioning actions on Russia at an unprecedented intensity and pace").

5 Kilcrease et al., *supra* note 4.

6 Clare Sebastian, *Ruble hits 8-month low against dollar, as falling oil prices and sanctions bite*, CNN (Dec. 29, 2022, 7:36 AM), https://www.cnn.com/2022/12/29/investing/ruble-dollar-russia-oil/index.html

exports allowed Russia to acquire foreign exchange and prop up the currency.[7]

The vigor with which international sanctions against Russia have been imposed has been tempered by concerns about global energy prices, inflation, and the prospect of an economic slowdown or recession.[8] The need to increase economic pressure on Russia while avoiding excessive harm to other economies has birthed novel sanctions mechanisms, including the freezing of Russian Central Bank assets and the use of European shipping and insurance industries to enforce a calibrated price cap on Russian oil exports.[9] These new approaches may be having their desired effect. In December 2022, the ruble fell to its lowest level against the dollar since April, likely due to falling oil prices and the effect of sanctions.[10]

But more could be done. In our article *Tax Law as Foreign Policy*, we argued that federal income tax law could play a greater role than it currently does in advancing U.S. foreign policy interests and complementing existing sanctions regimes.[11] Since writing that article, the economic sanctions imposed on Russia have made us more confident about the likelihood that tax will eventually step into this greater role, even if it does not play a significant part in ending the Russia-Ukraine conflict. One reason for our confidence is the opening of the Overton window in the world of economic sanctions over the last year, driven by the need to find additional and

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[https://perma.cc/CU3G-5AMK].

7 *Id.*

8 Jeff Stein & Emily Rauhala, *Global economic tremors complicate Western leaders' Russia sanctions*, WASH. POST (May 18, 2022, 5:17 PM), https://www.washingtonpost.com/us-policy/2022/05/18/russia-energy-west-economy-sanctions/ [https://perma.cc/7UED-VDYE] ("Growing fears of a global economic slowdown are complicating Western allies' financial campaign against Russia, as world leaders struggle to craft new punishments for Moscow without compounding inflation and other domestic challenges.").

9 *See infra* Part II.B.

10 Sebastian, *supra* note 6.

11 Deeks & Hayashi, *supra* note 1, at 276 ("We argue that tax law holds promise to advance U.S. foreign policy interests and that it is especially important to deploy tax tools now. Tax law has distinctive features that make it both a partial substitute and a partial complement to other tools of economic coercion, which means that it can extend the influence of U.S. economic power while reducing the risk of overusing other economic tools."). We recognize that tariffs are an existing form of taxation on the imports of goods, but we focus in our work on the federal income tax.

alternative points of leverage over Russia. Another reason is the institutional capacity being developed both in the United States and elsewhere to enforce these novel economic sanctions.[12] But the most obvious reason to be bullish on the future role of tax sanctions as a tool of U.S. foreign policy is the fact that members of the U.S. Senate and House in the summer of 2022 made legislative proposals for tax sanctions.[13] These proposals would target Russia and Belarus with many of the tax sanctions we considered in our article, and others that we did not.

In this essay, we summarize our case for tax sanctions and describe the array of other sanctions that the United States and other states have imposed on Russia. We describe and evaluate the discussion draft of a tax sanctions regime for Russia and Belarus offered by Senators Wyden and Portman. Finally, we describe several other recent and important developments in domestic and international tax and trade law and explore their implications for the future of tax sanctions.

II. Tax Sanctions

In *Tax Law as Foreign Policy*, we offered several arguments for making greater use of the federal income tax as an instrument of U.S. economic statecraft and foreign policy—as an alternative or additional mechanism for sanctioning foreign targets. In some cases, we envisioned revising existing rules that already implement U.S. foreign policy objectives. In other cases, we envisioned adding new rules under federal income tax law that could be used to exert leverage over foreign actors. In this Part, we briefly summarize our recommendations for tax sanctions and their justifications. In Parts IV and V, we reconsider these recommendations and justifications in light of developments from the past year.

A. Recommendations

We begin by distinguishing between tax penalties imposed on U.S. persons transacting with foreign targets ("outbound tax sanctions"), and taxes imposed on the income of foreign targets that is connected to the United States in some way ("inbound tax sanctions"). The reach of the U.S. income tax is long, generally grasping all the income of U.S. persons—corporations, citizens, and

12 See *infra* Part V.

13 *See infra* Part IV.A.

resident aliens—and even income of foreign persons if that income is earned from U.S. sources or is connected to a U.S. business.[14] The former can be made subject to outbound tax sanctions while the latter can be made subject to inbound tax sanctions.

1. Outbound Tax Sanctions

Outbound tax sanctions already exist in the Internal Revenue Code (the "Code").[15] Perhaps the most important example is the treatment of U.S. persons who earn income from states that the United States does not recognize or conduct diplomatic relations with, or that sponsor terrorism.[16] Such states are listed in Section 901(j) of the Code and so we refer to such listed states as "Section 901(j)" states. Foreign taxes paid to Section 901(j) states that would otherwise entitle the taxpayer to a credit against their U.S. tax liability are not eligible for a credit.[17]

By disallowing the foreign tax credit for such income, income from Section 901(j) states can be subject to double taxation—both U.S. and foreign income taxes—thereby increasing the effective tax rate on that income and making it less attractive to do business in these states.[18] To the extent that denying credits discourages U.S. businesses from operating in Section 901(j) states, outbound tax sanctions deprive these states of the tax revenue that they might otherwise receive from U.S. businesses as well as the economic benefits—jobs and investment—generated by the businesses themselves. Thus, although the Code nominally imposes a tax on U.S. businesses for operating in Section 901(j) states, the Section 901(j) state itself is the economic target of the sanction.

Businesses earning income in Section 901(j) states are subject

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14 Ruth Mason, *Citizenship Taxation,* 89 S. CAL. L. REV. 169, 179-80 (2015) ("Like many countries, the United States taxes the worldwide income of residents . . . . But in addition to those physically present, and contrary to the practice of other countries, the United States also taxes its citizens and lawful permanent residents (greencard holders) on their worldwide income."); *see also* I.R.C. § 872(a)(2) (gross income of nonresident aliens includes income effectively connected to a U.S. trade or business).

15 Deeks & Hayashi, *supra* note 1, at 316.

16 I.R.C. § 901(j)(2)(A).

17 *Id.* § 901(j)(1).

18 Joseph Isenbergh, *The Foreign Tax Credit: Royalties, Subsidies, and Creditable Taxes*, 39 TAX L. REV. 227, 227 (1984) ("In broad outline, the credit prevents double taxation of overseas business operations by reducing the U.S. tax on foreign income by the amount of income tax paid to foreign governments.").

to a second tax sanction as well. Consider a foreign corporation with significant U.S. shareholders (specifically, U.S. shareholders who own at least 10% of the stock in the foreign corporation). For years before 2018, the active business income of such foreign companies that was earned in the state in which they were organized was generally not subject to U.S. federal income tax until that income was distributed to the U.S. shareholders.[19] By deferring the U.S. tax owed on this income until it was repatriated to the United States, this rule generally lowered the tax burden on that income and gave U.S. multinationals a strong incentive to earn income through subsidiaries in low-tax jurisdictions and delay distributing income from those subsidiaries.[20] However, if the income was earned from a Section 901(j) state, then the income was taxed to the corporation's significant U.S. shareholders just *as if* it had been actually distributed to them.[21]

For these two reasons, then, being listed in Section 901(j) has made it difficult for a state to attract business from U.S. firms. The outbound tax sanctions under Section 901(j) work best when U.S. businesses are sensitive to the additional tax burden created by the loss of foreign tax credits and the loss of the benefits of deferral, and when the U.S. taxpayer can divest from the target state with relative ease. Outbound sanctions are also well suited for a long-term strategy focused on weakening or containing the target state's economic development and capacities.[22]

Currently, states make their way onto the Section 901(j) list through decisions taken by the Executive, such as when the Executive severs diplomatic relations or the Secretary of State designates the state as providing support for acts of terrorism.[23] In order to remove a state from Section 901(j), the Secretary of State

19 *Tax Cuts and Jobs Act: A Comparison for Large Businesses and International Taxpayers*, IRS (June 21, 2022), https://www.irs.gov/newsroom/tax-cuts-and-jobs-act-a-comparison-for-large-businesses-and-international-taxpayers [https://perma.cc/L 3YT-KJPG].

20 James R. Hines Jr. & R. Glenn Hubbard, *Coming Home to America: Dividend Repatriations by US Multinationals*, in TAXATION IN THE GLOBAL ECONOMY 161, 163 (Assaf Razin & Joel Slemrod eds., 1990) ("The deferral of U.S. taxation creates an incentive for firms to delay paying dividends from their subsidiaries to their American parents.").

21 I.R.C. §§ 951(a)(1), 952(a)(5).

22 Deeks & Hayashi, *supra* note 1, at 317.

23 I.R.C. § 901(j)(2)(A).

must make a certification to the Secretary of the Treasury.[24] The President can also waive the tax credit sanction by making a determination that it is in the national interest of the United States to do so and that the waiver would expand trade or investment opportunities in the Section 901(j) state.[25] Our view is that this is a prudent approach in terms of delegations to relevant Departments within the executive branch, leaving important decision-making power over foreign policy in the hands of the President and the State Department while requiring some reason-giving for the determination. Other approaches are, of course, possible. Congress could, for example, change the Code to specifically list certain states—hard-wiring Section 901(j) status for those states.

Significant changes to the U.S. international tax rules made in 2017 now subject active business income of foreign subsidiaries to current U.S. taxation—albeit at a rate lower than 21%—even if the income is not earned in a Section 901(j) state.[26] By eliminating the benefit of deferral that previously existed, and by lowering the top U.S. corporate tax rate from 39% to 21%, these changes reduced some of the punitive effects of Section 901(j) outbound tax sanctions.[27] As we will discuss in Part V, very recent developments in the taxation of international income have likely eroded the effectiveness of these tax sanctions even further. We do not think this was intentional.

In general, the foreign policy goals of the U.S. income tax seem to be overlooked, and domestic and global tax policy reforms can inadvertently undermine the pursuit of these goals. These concerns have been validated by developments in the international tax space over the last 12 months.[28] In *Tax Law as Foreign Policy*, we argued for decoupling the foreign policy provisions of U.S. income tax law from the rest of the Code as much as possible, to reduce the likelihood that tax reform will have unintended consequences on U.S. foreign policy, and to pay greater attention to the foreign policy

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24 *Id*. § 901(j)(2)(B)(ii).

25 *Id*. § 901(j)(5)(A)(i).

26 We refer here to the taxation of "Global Intangible Low-Taxed Income," which is generally eligible for a deduction that lowers the effective tax rate on that income. *See* I.R.C. § 250.

27 See *infra* Part V.

28 *Id*.

implications of rulemaking.[29]

Denying foreign tax credits or ending deferral are not the only ways of increasing the tax costs of doing business in a foreign target state, and we can easily imagine simple alternatives. The most direct way of doing this would be to increase the tax rate applicable to income earned in those states. The U.S. corporate tax rate is currently 21%.[30] This rate could be higher for income earned in Section 901(j) states. Moreover, the higher rate could apply to all income earned in a Section 901(j) state, or it could be used to target certain industries or forms of economic activity. For example, a higher tax rate on interest, dividends, and capital gains from a tax-sanctioned state could be used to discourage passive investment in the state—thereby raising the cost of capital to businesses in that state—while having limited effect on direct investment by U.S. multinationals.

2. *Inbound Tax Sanctions*

Inbound tax sanctions apply to foreign persons earning income from U.S. sources or U.S. businesses.[31] Whereas outbound tax sanctions attempt to punish states indirectly by raising the cost to U.S. persons of doing business in those states, inbound tax sanctions apply directly to the foreign states, individuals, or entities themselves. Whereas outbound sanctions work best when U.S. persons have good alternative opportunities to doing business with the foreign target so that they will find it easier to divest and move their business elsewhere, inbound tax sanctions work best when the foreign target does *not* have good alternatives to investing in U.S. markets or operating their business in the United States. Inbound tax sanctions leverage the attractiveness of the U.S. economy as a place to invest, trade, and operate a business to generate pressure on foreign targets. When those targets cannot easily replicate the advantages of exposure to U.S. markets elsewhere, they will be willing to bear higher taxes to maintain that exposure. Without good alternative investment or trade options, inbound tax sanctions can

29 Deeks & Hayashi, *supra* note 1, at 316 ("The solution is to decouple foreign policy-related provisions from other tax rules, or for foreign policy to play a greater role in tax law, so that those undertaking tax reform are less likely to overlook those provisions.").

30 I.R.C. § 11(b).

31 Deeks & Hayashi, *supra* note 1, at 316.

impose greater costs that can only be relieved if the target changes its behavior to comply with U.S. foreign policy goals.

An example of an inbound tax sanction would be increasing the withholding tax otherwise applicable to payments of passive investment income—interest, dividends, rents, and royalties—from U.S. sources that are made to foreign persons.[32] The United States generally imposes a tax of 30% on such payments,[33] but there is an important exception for investors in debt of U.S. companies, which is known as the "portfolio interest exception."[34] Interest paid on bonds issued by U.S. corporations to foreign persons is generally exempt from this 30% tax, as long as the foreign persons are not significant U.S. shareholders of the U.S. corporation.[35] Increasing the tax rate on payments to a tax-sanctioned person above 30%, or denying them the portfolio interest exception, would be one way of imposing costs on the foreign target.

Inbound tax sanctions are likely to be more salient to the foreign target than outbound tax sanctions. In the case of outbound tax sanctions, the burden of compliance and remitting the tax falls on U.S. persons who are merely surrogates for the foreign target, which is the real object of the sanctions. A foreign target state that is subject to outbound tax sanctions is harmed indirectly, as U.S. investment is redirected—perhaps only slowly and partially—away to other states. By contrast, the obligation to pay inbound tax sanctions rests on the foreign target itself, such as the foreign individual or corporation, which will have more taxes withheld on their U.S.-source investment income or which will have to write a bigger check to the U.S. Treasury than it otherwise would.

3. Information Generation

Finally, we also observed in *Tax Law as Foreign Policy* that outbound tax sanctions could be used as an inducement for U.S. companies doing business in sanctioned states to collect and report information related to their businesses that might be useful for U.S. foreign policy makers. Our model for this idea is Section 999 of the

32 Deeks & Hayashi, *supra* note 1, at 318 ("An example of an inbound tax sanction would be an additional withholding tax on payments of interest, dividends, and royalties made to foreigners.").

33 I.R.C. §§ 871, 881.

34 *Id.* §§ 871(h), 881(c).

35 *Id.* §§ 871(h)(3), 881(c)(3).

Code. U.S. companies must report to the Internal Revenue Service ("IRS") if they have operations in, or related to, states—or nationals of those states—that require compliance with certain boycotts as a condition of doing business in that state.[36] U.S. companies must also report if they have been asked to participate in the boycott or if they have in fact agreed to participate in the boycott.[37]

At present, Section 999 only applies to the boycott of Israel by Iraq, Kuwait, Lebanon, Libya, Qatar, Saudi Arabia, Syria, and Yemen.[38] Information about the frequency of requests to comply with these national boycott laws can provide useful information about the ebb and flow of anti-Israeli sentiment in these states. We argued that the wide range of contacts that U.S. multinationals have in target states—with government officials, contractors, local businesses, and so on—allows them to collect information about on-the-ground sentiments that can be a useful complement to other forms of intelligence gathering. In a recent essay, Professor Claussen argues that we undersell the value of "tax intelligence," but that to realize its potential—and that of other information collected from the foreign commerce bureaucracy more generally—the U.S. government needs a regulatory framework for coordinating the collection, processing, and use of information generated by different agencies.[39]

B. Justifications

We offered three justifications for making greater use of federal income tax law as a tool of U.S. foreign policy and we framed our discussion in terms of the various hard choices and tradeoffs that must be made in this context.[40] The first tradeoff involves the fact that sanctions of all kinds harm domestic interests. They reduce the profitable trade and investment that would otherwise occur, and they impose compliance burdens on private sector actors to enforce the sanctions. The second tradeoff is with a political-economy risk. Sanctions can create domestic "winners," such as when tariffs or

36 *Id.* § 999(a)(1).

37 *Id.* § 999(a)(2).

38 List of Countries Requiring Cooperation with an International Boycott, 86 Fed. Reg. 18,374-18,375 (Apr. 8, 2021).

39 Kathleen Claussen, *Tax Intelligence*, 72 DUKE L.J. ONLINE 155, 159 & n.17, 168 (2023).

40 Deeks & Hayashi, *supra* note 1, at 316-29.

import bans stifle foreign competition for domestic producers. This dynamic creates the risk that foreign policy will be used as a fig leaf for protectionist impulses or used to cater to rent-seeking by domestic industries. Finally, there are concerns common to all sanctions regimes about the steps that foreign targets can take to evade the sanctions, the risk that the sanctions will outlive their usefulness, and the concern that targets lack a clear path to compliance that would end the sanctions. Tax sanctions are not a silver bullet for these concerns, but we continue to think that they can play a useful complementary role to the suite of existing tools of economic statecraft.

First, the expansive income tax jurisdiction of the United States means that tax sanctions can help reach individuals, states, and entities that are not easily targeted by existing sanctions. Export controls and tariffs affect cross-border trade in goods or services. Traditional sanctions only affect those with assets located in the United States or who wish to travel to the United States. The income tax reaches anyone who operates a business—or is deemed to operate a business by the activities of an agent working on their behalf—in the United States or who earns investment income from a U.S. corporation or other U.S. source.

The United States taxes all U.S. citizens and residents on their worldwide income, as well as foreign persons with income from U.S. sources and foreign persons with U.S. businesses, regardless of the nature of their economic activities, the banks they use to clear transactions, or the currencies they transact in.[41] Moreover, while foreign persons earning only passive investment income have their income taxes withheld by the payor, foreign persons with U.S. businesses must file a U.S. tax return, which includes information that could be useful to foreign policymakers.

Second, merely introducing a new tool in the sanctions tool kit allows U.S. policymakers to operate on different points of leverage over foreign targets and take some of the pressure off existing sanctions tools. Although we do not think there is any imminent threat to the U.S. dollar as a global reserve currency or the U.S. financial system for clearing international transactions, we also do not think that it is prudent to entirely ignore the risk that states concerned about U.S. sanctions will find ways to avoid relying on the dollar and U.S. banks. As we discuss below, since 2014 Russia

41 *See id.* at 278 n.5.

has been particularly innovative in finding ways to avoid exposure to U.S. sanctions mechanisms. Moreover, it remains unclear what role China and the renminbi will occupy in the global financial landscape in the medium and longer term, and it would be wise to plan for a world in which the U.S. financial role is less hegemonic.

Third, income tax law provides considerable flexibility to modulate the pressure placed on foreign targets, allowing the pressure to be dialed up or down in degrees—through increments in the tax rate—rather than merely flipped on or off. Tax sanctions are not outright prohibitions on certain activities, but they increase the costs of doing business. As a result, they may be less salient and generate less backlash from both foreign targets and taxpayers in allied states than secondary sanctions, which have proven controversial with U.S. allies. Whether this modulation is done by the executive or Congress would depend on how the statute is drafted. The authority to adjust sanctions rates could be delegated to the president, or it could be fixed by the statute, in which case Congressional action would be required to make any the adjustments. We suspect that giving the executive the authority to change not only who is subject to tax sanctions but also the severity of those sanctions would be desirable because of the speed of executive action and the executive's foreign policy and economics expertise.

The field of economic sanctions has become more crowded in the past year, with old tools seemingly being used on more targets than ever and new tools of economic influence being conceived and implemented. In the next Part we describe the explosion of economic sanctions against Russia, but in doing so reveal that there is still room for tax sanctions.

III. Russia Sanctions

In response to Russia's invasion of Ukraine, the United States, the European Union ("EU"), and other allies such as Canada and Australia have made unprecedented, swift, and severe use of the tools of economic statecraft.[42] These states have turned to a

42 For comprehensive surveys of the economic tools that the United States, the EU, and other allies have deployed against Russia, see, e.g., Scott R. Anderson et al., *What Sanctions Has the World Put on Russia?*, LAWFARE (Mar. 4, 2022), https://www.lawfareblog.com/what-sanctions-has-world-put-russia [https://perma.cc/3ZSG-VLKS]; CONG. RES. SERV., *Russia's 2022 Invasion of Ukraine: Overview of U.S. Sanctions and Related Responses* (2022),

strikingly broad range of tools in their all-out effort to punish the Russian government's leadership, hinder the Russian military's ability to fight the conflict in Ukraine, cut off funds and technologies to those parts of the Russian economy that are supporting the war, and show strong condemnation of this blatant act of aggression. Ultimately, these states may be trying to weaken Russia to such an extent that it will not be in a position to invade a neighboring state again.[43]

Many of the tools these states are using are familiar: economic sanctions, export and import controls, and trade controls. Some are more novel, including cutting off Russian banks' access to SWIFT, freezing Russian Central Bank assets, and imposing price caps on Russia's oil exports.[44] At each turn, the United States and the EU have had to wrestle with two confounding factors. First, they must develop these restrictions with an eye toward whether and how Russia can evade them. Second, the United States and EU are keenly aware that the economic restrictions on Russia may, if not appropriately calibrated, adversely affect the West's own domestic goals, which include ensuring adequate energy supplies, avoiding excessive inflation, and keeping consumer gas prices affordable. Interestingly, amid all the creative tools that the United States and its allies have deployed in an effort to balance these factors, none has involved the income tax.

A. Traditional Tools

The United States imposed a range of sanctions on Russia after it invaded Crimea in 2014 and attempted to interfere in the 2016 U.S. presidential elections.[45] Beginning on the eve of the 2022

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https://crsreports.congress.gov/product/pdf/IN/IN11869 [https://perma.cc/NZP9-6Z4H]; Chad P. Brown, *Russia's War on Ukraine: A Sanctions Timeline*, PETERSON INST. FOR INT'L ECON.: REALTIME ECON. (Feb. 27, 2023, 4:40 PM), https://www.piie.com/blogs/realtime-economic-issues-watch/russias-war-ukraine-sanctions-timeline [https://perma.cc/M32S-YDKT]; and Kilcrease et al., *supra* note 4. For commentary on how the response "has constituted a sea change in sanctions practice globally," see Oscar, *supra* note 4.

43 Kilcrease et al., *supra* note 4 ("[B]oth U.S. Secretary of Defense Lloyd Austin and U.S. Secretary of State Antony Blinken expressed intent to weaken the Russian military to a point where it no longer has the capability to invade its neighbors.").

44 For an overview of the sanctions now in place, *see generally* Don S. De Amicis & David P. Stewart, *Sanctions on Steroids: The Ukraine-/Russia-Related Sanctions*, 48 N.C. J. INT'L L. 379 (2023).

45 *See* Exec. Order No. 13660, 3 C.F.R. 226 (2014) (Crimea); Exec. Order No. 14024,

invasion of Ukraine and continuing to the present, the United States used both existing and new executive orders to freeze assets and block U.S. financial transactions with the breakaway Ukrainian territories of Donetsk and Luhansk;[46] Russian financial institutions;[47] certain Russian companies; Russian elites linked to Vladimir Putin, such as the director of the Federal Security Service and senior executives at Russian banks;[48] and 340 members of Russia's Duma.[49] The United States has also imposed secondary sanctions on individuals and companies (both inside and outside Russia) who are providing material support to Russia in its illegal efforts to annex Ukrainian territory.[50] For example, the United States has imposed secondary sanctions on Iranian companies selling and transporting drones to Russia[51] and on Chinese and Armenian companies that supplied a Russian defense procurement company.[52] Many companies have also "self-sanctioned," reducing their corporate involvement in Russia, even if their business there

86 Fed. Reg. 20,249 (2021) (malign international conduct).

46 Exec. Order No. 14024, *supra* note 45; Exec. Order No. 14065, 87 Fed. Reg. 10,293 (2022).

47 U.S. Dep't of the Treasury, Russia-related Designations (Feb. 22, 2022), https://home.treasury.gov/policy-issues/financial-sanctions/recent-actions/20220222 [https://perma.cc/RQR2-PFHP] (designations on VEB.RF, Promsvyazbank, and VTB).

48 *Id.* (designations of Denis Bortnikov, Petr Fradkov, and Vladimir Kiriyenko).

49 Press Release, Antony J. Blinken, Sec. of State, Sanctioning Additional Members of Russia's Duma, Russian Elites, Bank Board Members, and Defense Entities (Mar. 24, 2022), https://www.state.gov/sanctioning-additional-members-of-russias-duma-russian-elites-bank-board-members-and-defense-entities/ [https://perma.cc/BH85-T3ET].

50 U.S. Dep't of the Treasury, FAQ: Russian Harmful Foreign Activities Sanctions, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/1091 [https://perma.cc/3MRR-Y7LH] (noting the use of Executive Orders 13660, 14024, and 14065, which authorize the U.S. government to impose blocking sanctions on certain categories of people).

51 Julian E. Barnes, *The U.S. Announces Sanctions on Iranian Companies Involved in Russia Drone Sales*, N.Y. TIMES (Sept. 8, 2022), https://www.nytimes.com/2022/09/09/world/europe/08ukraine-briefing-iran-drones-sanctions.html_[https://perma.cc/5GFV-4QMT]; John Irish & Philip Blenkinsop, *EU to Add* New *Iran Sanctions Over Drone* Supplies *to Russia*, REUTERS (Oct. 19, 2022), https://www.reuters.com/world/eu-set-sanction-8-people-entities-over-iranian-drone-use-ukraine-diplomats-2022-10-19/ [https://perma.cc/XU2T-94WH].

52 U.S. Dep't of the Treasury, Russia-related Designations and Designations Updates; Publication of Russia-related Frequently Asked Questions (Sept. 30, 2022), https://home.treasury.gov/policy-issues/financial-sanctions/recent-actions/20220930 [https://perma.cc/K4JH-AYTR].

does not directly implicate sanctioned individuals.[53] However, a range of U.S. companies continue to do business in Russia—and a number of U.S., British, and German citizens continue to serve on boards and in executive positions at Russian companies—which means income tax sanctions would still have utility.[54]

In addition to these sanctions, the United States has imposed a large number of export controls in an effort to degrade Russia's military capabilities and prevent Russia from being able to use U.S.-made items in its war against Ukraine.[55] Using authorities in the Export Control Reform Act of 2018, the Biden Administration has "[d]enied all [U.S.] exports, reexports to, and transfers of items subject to the Export Administration Regulations for military end uses or end users in the Russian Federation and Belarus."[56] The Administration has also prohibited the export of luxury goods or accounting, corporate formation, or management consulting services from the United States to any person in Russia[57] and denied exports of items needed for oil refining.[58] It has not acted alone: 37 states have applied substantially similar controls "to isolate Russia

53 Kilcrease et al., *supra* note 4. For overviews of "self-sanctioning," see Adam M. Smith & Cody M. Poplin, *Keeping Sanctions "Smart": Calibrating U.S. Sanctions Policy to Overcome Overcompliance*, 48 N.C. J. INT'L L. 499 (2023); Pierre-Hugues Verdier, *Sanctions Overcompliance: What, Why, and Does It Matter?*, 48 N.C. J. INT'L L. 471 (2023).

54 *See* Kate Gibson, *These U.S. Companies Are Still Doing Business in Russia*, CBS NEWS (May 24, 2022), https://www.cbsnews.com/news/us-businesses-still-in-russia-ukraine-sbarro-hard-rock-cafe-mcdonalds-starbucks-koch/ [https://perma.cc/S82M-DL88] (listing Hard Rock Café, Sbarro, Match.com, and Domino's as continuing to do business as of May 2022); Alistair MacDonald & Ben Dummett, *Ukraine Denounces Western Executives at Russian Companies; Kyiv Says Presence of Foreign Business Leaders Lends Credibility to Moscow's War Effort*, WALL ST. J. (Feb. 1, 2023), https://www.wsj.com/articles/ukraine-denounces-western-executives-at-russian-companies-11675202772 [https://perma.cc/J37V-57FQ].

55 Maia Nikoladze, *US Export Controls Aim to Degrade Russia's Military*, ATL. COUNCIL (Mar. 18, 2022), https://www.atlanticcouncil.org/blogs/econographics/us-export-controls-aim-to-degrade-russias-military/ [https://perma.cc/C9HD-4AH6].

56 Fact Sheet, U.S. Dep't of State, The Impact of Sanctions and Export Controls on the Russian Federation (Oct. 20, 2022), https://www.state.gov/the-impact-of-sanctions-and-export-controls-on-the-russian-federation/ [https://perma.cc/WC2U-F3XL].

57 International Trade Administration, *Professional Services News: United States Bans Certain Services Exports to Russia*, INT'L TRADE ADMIN. (last visited Mar. 12, 2023), https://www.trade.gov/feature-article/professional-services-news-united-states-bans-certain-services-exports-russia [https://perma.cc/TUF8-XZ6L] (relying on Exec. Orders 14071 and 14024).

58 Fact Sheet, U.S. Dep't of State, *supra* note 56.

from commodities, technologies, and software necessary for Putin's war."[59]

The United States has gone further, prohibiting imports into the United States of oil, seafood, alcoholic beverages, and certain other products of Russian origin.[60] It also has banned Russian ships from entering U.S. ports, though less than 1% of the cargo that arrives at U.S. ports comes on Russian-flagged vessels.[61] And for many products destined for Russia the Commerce Department has deployed the "foreign direct product rule," pursuant to which products that are made outside the United States, but directly use U.S. software or technology, can be subject to U.S. re-export control laws.[62]

Finally, the United States and EU have used trade tools to increase pressure on Russia. The U.S. Congress passed a law authorizing the President to suspend normal trade relations with Russia (and Belarus), which denies "most favored nation" tariff treatment to those states, and which will result in higher duties on products imported from them.[63] The EU had earlier dropped Russia's "most favored nation" designation. Of course, the resulting increase in tariffs will be reciprocal: As the damage to Russia goes up, the states imposing these restrictions will feel more pain too.[64]

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59 *Id.*

60 Exec. Order No. 14068, 87 Fed. Reg. 14,381 (Mar. 11, 2022).

61 *See* White House, A Proclamation on the Declaration of National Emergency and Invocation of Emergency Authority Related to the Regulation of the Anchorage and Movement of Russian-Affiliated Vessels to U.S. Ports (Apr. 21, 2022), https://www.whitehouse.gov/briefing-room/presidential-actions/2022/04/21/a-proclamation-on-the-declaration-of-national-emergency-and-invocation-of-emergency-authority-relating-to-the-regulation-of-the-anchorage-and-movement-of-russian-affiliated-vessels-to-united-states-po/ [https://perma.cc/BAS6-BNWR]; Nancy Youssef & Costa Paris, *Biden Expected to Ban Russian Ships From Entering U.S. Ports*, WALL ST. J. (Mar. 2, 2022), https://www.wsj.com/articles/biden-expected-to-ban-russian-ships-from-entering-u-s-ports-11646247671 [https://perma.cc/U98C-UKZP].

62 Foreign-Direct Product Rules, 15 C.F.R. § 734.9 (2023); U.S. Dep't of Commerce, Fact Sheet (Feb. 2022), https://www.bis.doc.gov/index.php/documents/about-bis/newsroom/press-releases/2913-2022-02-24-bis-russia-rule-fact-sheet-final/file [https://perma.cc/W5RY-5NF6].

63 Suspending Normal Trade Relations with Russia and Belarus Act, Pub. L. No. 117-110, 136 Stat. 1159 (2022).

64 Charles Hankla, *Russia's No Longer a 'Most-Favored Nation': 5 Questions About the Coveted Trading Status Answered*, CONVERSATION (Mar. 17, 2022), https://theconversation.com/russias-no-longer-a-most-favored-nation-5-questions-about-the-coveted-trading-status-answered-179185 [https://perma.cc/7NHF-Y6EU].

B. Bespoke Tools

In addition to using the traditional set of sanctions, export and import controls, and tariffs to adversely affect Russia's ability to fight, the United States and its allies have deployed more unusual, sometimes bespoke tools to achieve that goal. These tools include freezing Russian Central Bank assets, cutting off Russian banks from SWIFT, restricting Russia's ability to issue sovereign debt, and imposing a price cap on Russian oil and gas exports.

1. Russian Central Bank Assets

Both the United States and various states in Europe have taken the significant step of freezing Russian Central Bank assets in their jurisdiction. On February 26, 2022, these states committed to "imposing restrictive measures that will prevent the Russian Central Bank from deploying its international reserves in ways that undermine the impact of our sanctions."[65] To implement that commitment in the United States, the Office of Foreign Assets Control issued a directive prohibiting U.S. persons from undertaking transactions with the Central Bank of Russia, Russia's National Wealth Fund, or Russia's Ministry of Finance, "including any transfer of assets to such entities or foreign exchange transaction."[66] This made it difficult for Russia to access its foreign reserves and thus hindered the Central Bank's ability to stabilize the ruble.

As Scott Anderson noted, this is a dramatic step, one that the United States previously has used only against hostile foreign regimes such as in Iran, Syria, and North Korea.[67] The Biden Administration apparently is debating whether it has statutory authority to undertake an even more aggressive measure: seizing $38 billion of Russian Central Bank assets in the United States and

65 White House, Joint Statement on Further Restrictive Economic Measures (Feb. 26, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/02/26/joint-statement-on-further-restrictive-economic-measures/ [https://perma.cc/ST9Q-NAJS].

66 Off. of Foreign Assets Control, U.S. Dep't of the Treasury, Directive 4 Under Executive Order 14024: Prohibitions Related to Transactions Involving the Central Bank of the Russian Federation, the National Wealth Fund of the Russian Federation, and the Ministry of Finance of the Russian Federation (Feb. 28, 2022), https://home.treasury.gov/system/files/126/eo14024_directive_4_02282022.pdf [https://perma.cc/CKW3-3HFH].

67 Anderson et al., *supra* note 42.

giving the funds to Ukraine to help it rebuild.[68] It is unclear whether the Administration plans to pursue this option, which would raise concerns under international law.

2. Removing Russia from SWIFT

SWIFT is a financial transaction processing system based in Belgium, which thousands of financial institutions use to facilitate their cross-border money transfers.[69] Removing a state's banks from SWIFT therefore has a significant impact on its international trade. Because it is a harsh tool, there is only limited precedent for its use: states banned Iran from SWIFT in 2012 as a sanction for its nuclear activities.[70]

On March 1, 2022, the EU, United Kingdom, United States, and Canada agreed to remove seven of Russia's banks from the SWIFT system.[71] They did not remove Russia's largest bank, Sberbank, from SWIFT at that time, for fear that doing so would create turmoil in global energy markets.[72] However, in June 2022, the EU ultimately agreed to remove Sberbank and two other Russian banks from SWIFT,[73] with the goal of further isolating the Russian

68 Paul Stephan, *Giving Russian Assets to Ukraine—Freezing Is Not Seizing*, LAWFARE (Apr. 26, 2022, 10:48 AM), https://www.lawfareblog.com/giving-russian-assets-ukraine-freezing-not-seizing [https://perma.cc/62KA-RN2A]; Scott R. Anderson & Chimène Keitner, *The Legal Challenges Presented By Seizing Frozen Russian Assets*, LAWFARE (May 26, 2022, 3:09 PM), https://www.lawfareblog.com/legal-challenges-presented-seizing-frozen-russian-assets [https://perma.cc/U4CE-TAQU].

69 *Swift History*, SWIFT, https://www.swift.com/about-us/history [https://perma.cc/5BF2-CPFG] (last visited Mar. 13, 2023).

70 Russell Hotten, *Ukraine conflict: What is Swift and why is banning Russia so significant?*, BBC (May 4, 2022), https://www.bbc.com/news/business-60521822 [https://perma.cc/E3J5-YPJP]; Swift, *Does Swift Expel Banks?*, SWIFT, https://www.swift.com/about-us/legal/compliance-0/swift-and-sanctions#does-swift-expel-banks? [https://perma.cc/PJ3N-X5QE] (last visited Mar. 13, 2023).

71 Alberto Nardelli, Nikos Chrysoloras & John Follain, *EU to Ban Seven Russian Banks From SWIFT, Spare Key Firms*, BLOOMBERG (Mar. 1, 2022, 1:17 PM), https://www.bloomberg.com/news/articles/2022-03-01/eu-agrees-to-block-russian-banks-from-swift-sparing-key-firms [https://perma.cc/V876-JBGQ].

72 Christian Perez, *What Does Russia's Removal From SWIFT Mean For the Future of Global Commerce?*, FOREIGN POL'Y (Mar. 8, 2022), https://foreignpolicy.com/2022/03/08/swift-sanctions-ukraine-russia-nato-putin-war-global-finance/ [https://perma.cc/Z4X6-7EU4].

73 Jan Strupczewski, *EU to remove Sberbank, two other Russian banks from SWIFT,* REUTERS (May 3, 2022, 11:54 PM), https://www.reuters.com/business/finance/eu-remove-sberbank-two-other-russian-banks-swift-2022-05-04/ [https://perma.cc/R4ZD-

financial sector from the international banking system.

3. Sovereign and Corporate Debt

The United States also restricted the ability of Russia's Central Bank, National Wealth Fund, and Ministry of Finance to obtain funding by issuing sovereign debt. It did so by restricting purchases by U.S. financial institutions of bonds issued by those Russian entities and lending to those entities.[74] The Treasury Department later expanded these restrictions to purchases of anything other than short-term debt or equity from other named financial institutions and leading companies in sectors such as oil, gas, maritime shipping, and telecommunications.[75] As Scott Anderson et al. noted, "Together, these sanctions put major constraints on these Russian institutions' ability to receive loans and shrink the global market for—and thus the value of—any debt instruments they may offer or already have in circulation. This promises to make it substantially harder for the businesses to raise capital needed to operate or expand."[76]

4. Russian Energy Import Bans and Oil Price Caps

Russia is a major energy exporter: in 2021, revenues from oil and gas exports made up 45 percent of Russia's federal budget[77] and 60 percent of its national exports.[78] At the same time, EU member

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P6GC]; Laurence Norman, *EU to Remove Russia's Biggest Bank From Swift Network*, WALL ST. J. (July 2, 2022, 5:35 PM), https://www.wsj.com/livecoverage/russia-ukraine-latest-news-2022-06-02/card/eu-to-remove-russia-s-biggest-bank-from-swift-network-MaOJ54J37GOZ6f96v507 [https://perma.cc/6HDY-8MXC].

74 Off. of Foreign Assets Control, U.S. Dep't of the Treasury, Directive 1A Under Executive Order 14024: Prohibitions Related to Certain Sovereign Debt of the Russian Federation (Feb. 22, 2022), https://home.treasury.gov/system/files/126/russia_directive_1a.pdf [https://perma.cc/78XQ-EP42].

75 Off. of Foreign Assets Control, U.S. Dep't of the Treasury, Directive 3 Under Executive Order 14024: Prohibitions Related to New Debt and Equity of Certain Russia-related Entities (Feb. 24, 2022), https://home.treasury.gov/system/files/126/new_debt_and_equity_directive_3.pdf [https://perma.cc/G7RE-AGGR].

76 Anderson et al., *supra* note 42.

77 *Energy Fact Sheet: Why does Russian oil and gas matter?*, IEA (Mar. 21, 2022), https://www.iea.org/articles/energy-fact-sheet-why-does-russian-oil-and-gas-matter [https://perma.cc/G65L-DFX5].

78 Kilcrease et al., *supra* note 4.

states rely heavily on Russian oil and gas, which makes up about 40% of their consumption.[79] As a result, the United States and its allies have worked very hard to find ways to reduce Russia's oil profits without leaving European states short of gas supplies or harming their economies more generally.

Because the United States does not rely heavily on Russian oil and gas, it was able to quickly ban the import of Russian oil, natural gas, and coal.[80] The EU took longer to do so. In late May 2022, the EU finally banned the import of all seaborne oil and agreed to wind down 90% of imports of Russian oil by the end of 2022.[81]

But that still left open a window for Russia to continue to make significant oil revenue from sales to other states. Thus, in September 2022, the G-7 states—the United States, Japan, Canada, France, Italy, Germany, and the United Kingdom—announced that they would limit the ability of Russia to sell oil above a specified price.[82] The mechanism for capping the sales price of Russian oil leverages the dominance of the UK maritime insurance industry and European shipping by prohibiting these companies from insuring and transporting shipments of oil sold above a specified price.[83] The purpose of the cap is to limit a crucial source of Russia's revenues and hence its ability to continue to wage war in Ukraine, as well as to harm the Russian economy more generally, without cutting off Russian oil exports altogether.[84] Thus, this approach is an attempt

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79 Anne-Sophie Corbeau, *How Deep Is Europe's Dependence on Russian Oil?*, COLUM. CLIMATE SCH. (Mar. 14, 2022), https://news.climate.columbia.edu/2022/03/14/qa-how-deep-is-europes-dependence-on-russian-oil/ [https://perma.cc/2YKG-GHGN].

80 Fact Sheet, White House, United States Bans Imports of Russian Oil, Liquefied Natural Gas, and Coal (Mar. 8, 2022), https://www.whitehouse.gov/briefing-room/statements-releases/2022/03/08/fact-sheet-united-states-bans-imports-of-russian-oil-liquefied-natural-gas-and-coal/ [https://perma.cc/98KM-A6A8] (noting that not all of the U.S. partners "are currently in a position to join us" in imposing this import ban).

81 Niamh Kennedy, *EU agrees on partial ban of Russian oil imports*, CNN (May 31, 2022, 12:25 PM), https://www.cnn.com/2022/05/30/energy/eu-russian-oil/index.html [https://perma.cc/A63J-HLJD].

82 Stein & Rauhala, *supra* note 8.

83 David Wessel, *The story behind the proposed price cap on Russian oil*, BROOKINGS INST. (July 5, 2022), https://www.brookings.edu/blog/up-front/2022/07/05/the-story-behind-the-proposed-price-cap-on-russian-oil/ [https://perma.cc/DXJ3-JNRX] (noting that European and British companies account for about 85-90% of insuring, reinsuring, and financing seaborne Russian oil).

84 Stein & Rauhala, *supra* note 8.

to place calibrated pressure on Russia—much in the same way that tax sanctions could—rather than an all-or-nothing approach that would impose greater costs on European industries and citizens.

In December 2022, the United States and the EU agreed on the price cap figure: $60 per barrel of crude oil.[85] Purchases of Russian oil for more than that amount are ineligible for shipping, insurance, and other services provided by G7 states.[86] The negotiations were difficult because European companies with large maritime industries were worried about the burdens on those companies to enforce the cap and their loss of revenue if the price cap were set too low.[87] The G7 also had to set the cap high enough that Russia could recover its production costs and therefore have an incentive to keep producing.[88] Some EU diplomats sought broader geographic support for the cap, including from China and India, for fear that those states would otherwise buy Russian oil at higher prices and sell it to third states at a premium.[89] Others feared that Russia would retaliate by further limiting natural gas sales to Europe, which faces winter shortages.[90] Although some Eastern European states argued that the price cap figure should be lowered significantly,[91] the G7 had not revised that figure as of March 2023.[92]

This nuanced approach to Russian oil and gas sales is reminiscent of our tax sanctions proposal. Indeed, Treasury

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85 Emily Rauhala et al., *Western nations agree to cap price of Russian oil at $60 a barrel*, WASH. POST (Dec. 2, 2022).

86 *Questions and Answers: G7 agrees oil price cap to reduce Russia's revenues, while keeping global energy markets stable,* EUROPEAN COMM'N (Dec. 3, 2022), https://ec.europa.eu/commission/presscorner/detail/en/QANDA_22_7469 [https://perma.cc/92Y9-85T2].

87 Matina Stevis-Gridneff, Jim Tankersley & Alan Rappeport, *G7 and Allies Fail to Agree on Price Cap for Russian Oil*, N.Y. TIMES (Nov. 23, 2022), https://www.nytimes.com/live/2022/11/23/world/russia-ukraine-war-news [https://perma.cc/G8UX-VNV6].

88 Stein & Rauhala, *supra* note 8.

89 *Id.*

90 *Id.*

91 Richard L. Morningstar & Benjamin L. Schmitt, *Why the Oil Price Cap Won't Hurt Putin*, FOREIGN POL'Y (Dec. 15, 2022, 3:01 PM), https://foreignpolicy.com/2022/12/15/russia-ukraine-war-sanctions-oil-embargo-price-cap-putin-revenue-energy/ [https://perma.cc/VN7B-RKU8].

92 REUTERS, *G7 to Hold Off Revising Russian Oil Price Cap This Week – EU Officials* (Mar. 20, 2023), https://www.reuters.com/business/energy/g7-hold-off-revising-russian-oil-price-cap-this-week-eu-officials-2023-03-20/ [https://perma.cc/KFA5-WAV9].

Secretary Janet Yellen originally proposed that major importers impose a tariff on Russian oil.[93] Because there is a global market for oil, consumers would pay the world price, but Russia would only receive that price minus the tariff.[94] The effect of tariffs, and of the oil price cap, is to impose costs on a bad actor without barring the activity entirely – something tax sanctions do well.

C. Russia's Efforts to Evade Restrictions

Not surprisingly, in light of these multi-pronged efforts to squeeze Russia's economy and military machine, the United States and its allies have focused on ways that Russia might evade these tools of economic statecraft – and on ways to prevent it from doing so. This issue may become even more important as the conflict in Ukraine drags on, and evidence about Russia's ability to evade trade sanctions in co-operation with its allies mounts.[95]

Shortly after the Russian invasion, the United States helped organize a multi-national "Russian Elites, Proxies, and Oligarchs Task Force" to block or freeze more than $30 billion of sanctioned assets and promote effective sanctions implementation by financial institutions.[96] Domestically, the Department of Justice established "Task Force KleptoCapture" to enforce the range of economic countermeasures against Russia and its officials, including by prosecuting sanctions violators.[97]

Policymakers also have considered how Russia might avoid the strictures of the oil price cap, though it is too early to tell whether

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93 Secretary Yellen justified the cap both on foreign policy grounds and on the grounds that it would fight inflation and prevent future price spikes. Press Release, U.S. Dep't of the Treasury, Statement by Secretary of the Treasury Janet L. Yellen on the G7 Price Cap Announcement (Sept. 2, 2022), https://home.treasury.gov/news/press-releases/jy0936 [https://perma.cc/WF9C-FBLS].

94 Wessel, *supra* note 83.

95 Ana Swanson, *Russia Sidesteps Western Punishments, With Help From Friends*, N.Y. TIMES (Jan. 31, 2023), https://www.nytimes.com/2023/01/31/business/economy/russia-sanctions-trade-china-turkey.html [https://perma.cc/4SUY-UHUL].

96 Press Release, U.S. Dep't of the Treasury, Russian Elites, Proxies, and Oligarchs Task Force Joint Statement (June 29, 2022), https://home.treasury.gov/news/press-releases/jy0839 [https://perma.cc/TH99-2WN6].

97 Press Release, U.S. Dep't of Just., Attorney General Merrick B. Garland Announces Launch of Task Force KleptoCapture (Mar. 2, 2022), https://www.justice.gov/opa/pr/attorney-general-merrick-b-garland-announces-launch-task-force-kleptocapture [https://perma.cc/WAV7-R4J4].

Russia has deployed these options. First, it is possible that states such as China and India will continue to purchase Russian oil at market prices and re-sell that oil into the global market at elevated prices. Second, "Russia might agree to a cap of, say, $50 a barrel but deliver the oil only if a buyer in, say, India also agrees . . . to buy shiploads of used shoes or scrap paper worth another $50 a barrel."[98] Third, Russia might try to identify alternative shippers and insurers, though it is not clear that Russian, Chinese, or Indian insurers have the reputations and capacity to fill the gap.[99]

In a few areas, Russia had already prepared fallback alternatives to a benefit from which the West cut it off. In 2014, states had threatened to remove Russia from SWIFT; as a result, Russia created a substitute cross-border transfer system.[100] Although few states and foreign banks use it, Russia's Central Bank stated that the use grew considerably in 2022.[101] And Russia is trying to connect to China's cross-border SWIFT alternative, which processes payments in yuan.[102]

Russia had also taken steps to guard against sanctions in its bond market. Beginning in 2016, Russia began to include a novel provision in its bonds denominated in foreign currency.[103] This provision allows the Russian government to pay interest and principal using an alternate payment currency ("APC"), i.e., a currency other than the one in which the debt is denominated, if Russia cannot make payments in the currency in which the debt is denominated for "reasons beyond its control."[104] Since March 2018, these APC clauses have permitted Russia to make payments in rubles.[105] This contractual innovation allows Russia to avoid some of the negative consequences of financial sanctions. Whereas limiting Russia's access to U.S. dollars might have previously

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98 Wessel, *supra* note 83.

99 *Id.*

100 Hotten, *supra* note 70.

101 Alexander Marrow, *Russia's SWIFT Alternative Expanding Quickly This Year, Says Central Bank*, REUTERS (Sept. 23, 2022), https://money.usnews.com/investing/news/articles/2022-09-23/russias-swift-alternative-expanding-quickly-this-year-says-central-bank [https://perma.cc/UK5S-SFK3].

102 Hotten, *supra* note 70.

103 Michael Bradley et al., *A Silver Lining to Russia's Sanctions-Busting Clause?*, 108 VA. L. REV. ONLINE 326, 328 (2022).

104 *Id.*

105 *Id.* at 328-29.

prevented it from making scheduled payments on its international debt and pushed it into default, debt obligations containing the APC provision allow Russia to continue to make debt payment in its own currency. Markets have generally reacted favorably to this option.[106]

D. Room for Tax Sanctions

In our prior article, we noted that the use of the income tax as a foreign policy tool offers several advantages: the ability to reduce certain problematic activities without foreclosing them entirely; a lower salience than overt economic sanctions, export controls, and tariffs; and a domestic focus that can facilitate compliance and could ameliorate a desire to shift toward alternative currencies.[107] The economic statecraft in use against Russia since February 2022 helps us fine-tune these points. First, even when a coalition of states is firmly committed to halting another state's ability to sustain a war, economic interdependence and the need to balance punishment and self-harm means that there is still room for tools that allow for a nuanced, non-binary response to economic activity. The oil price cap offers a good illustration of this point.

Second, there obviously will be cases (like this one) in which states explicitly want their economic statecraft to have high salience, as a way to signal as much public opprobrium as possible. In those cases, the lower-salience nature of tax sanctions will be less important – and indeed may run counter to the sanctioning states' goals. Finally, to the extent that the United States and the EU wish to continue to explore different means by which to hinder Russia's military operations, they should consider the possible role for income tax tools. The next Part examines one congressional proposal to do this.

IV. Proposed Tax Sanction Legislation

A The Wyden-Portman Proposal

On April 7, 2022, Senators Wyden and Portman released a discussion draft of legislation (the "discussion draft") that would impose tax sanctions on a wide array of targets with connections to Russia and Belarus and on the governments of those states

106 *Id.* at 331, 342 (noting that the APC clauses appear to lower the yields on Russian debt).

107 Deeks & Hayashi, *supra* note 1, at 316-28.

themselves.[108] On June 1, companion legislation called the Support Ukraine Through Our Tax Code Act was introduced in the House of Representatives.[109] As of the time of writing, neither bill had become law. And although the Biden Administration does not appear to have weighed in on the proposal, we believe that it should give serious consideration to the use of tax sanctions as it searches for new legal tools to combat security threats.[110]

This Part summarizes the discussion draft offered by Senators Wyden and Portman and evaluates it in light of the considerations and ideas that we introduced in *Tax Law as Foreign Policy*. The discussion draft is important as a contemporary example of how a broad tax sanctions regime might look. It instantiates some of the ideas we discussed in our earlier article, introduces innovations that we did not consider, and resolves some of the tradeoffs that we identified in ways that merit further discussion. Although the tax sanctions would violate the U.S.-Russia income tax treaty, the draft legislation would override the treaty as a matter of domestic law.

The first tax sanction imposed by the discussion draft is to add the Russian Federation and the Republic of Belarus to the list of Section 901(j) states. As discussed in Part I, this would deny U.S. taxpayers the ability to claim a foreign tax credit for income taxes paid to these states[111] and would render income earned in Russia or Belarus by foreign corporations controlled by U.S. persons currently taxable to the corporation's significant U.S. shareholders.[112] The discussion draft provides an exception from

108 Press Release, U.S. Senate Committee on Finance, Wyden, Portman Release Bipartisan Bill to Disallow Foreign Tax Credits and Other Tax Benefits for Companies Operating in Russia (Apr. 7, 2022), https://www.finance.senate.gov/chairmans-news/wyden-portman-release-bipartisan-bill-to-disallow-foreign-tax-credits-and-other-tax-benefits-for-companies-operating-in-russia [https://perma.cc/HC69-FWZT].

109 Press Release, Congressman Jared Golden, For Country Caucus Members Introduce Bill to Exact Penalties on Businesses Still Operating in Russia (June 1, 2022), https://golden.house.gov/media/press-releases/for-country-caucus-members-introduce-bill-to-exact-penalties-on-businesses-still-operating-in-russia [https://perma.cc/6RMM-QMS7].

110 *See* David Lawder, *U.S. trade chief: new legal tools needed to combat future China threats*, REUTERS (May 13, 2021), https://www.reuters.com/world/us/us-trade-chief-tai-says-time-is-essence-china-trade-review-2021-05-13/ [https://perma.cc/X8LT-KFNW].

111 *See generally* Sen. Wyden and Sen. Portman, Discussion Draft, 117th Cong. § 1(a)-(b) (2022). We assume that the draft intends to deny a deduction for taxes paid to these states as well, although it is not clear that the draft language accomplishes this.

112 *Id.* at § 1(a) (adding Russia and Belarus to the list of Section 901(j) countries);

Section 901(j) for companies that wind down their activities—measured in terms of revenues—in Russia and Belarus sufficiently quickly.[113]

Russia or Belarus would be removed from Section 901(j) when the United States normalized trade relations with that state pursuant to the terms of section 4(b) of the Suspending Normal Trade Relations with Russia and Belarus Act (the "Trade Suspension Act").[114] That section delegates to the President the power to resume normal trade relations upon the submission to Congress of a certification that Russia or Belarus has reached an agreement regarding the withdrawal of troops and cessation of hostilities "that is accepted by the free and independent government of Ukraine," that it poses no immediate military threat to a NATO member, and that recognizes the right of Ukraine to choose its own government.[115] Before submitting the certification, the President must consult with the House Committee on Ways and Means and the Committee on Foreign Affairs, and the Senate Finance and Foreign Relations Committees, and submit to them a report explaining the basis for the President's determination.[116] Moreover, if Congress enacts into law a joint resolution of disapproval of the certification in the 90 days after submission of the certification, it will not take effect.

The discussion draft also imposes inbound tax sanctions. Specifically, the draft proposes taxing the Russian and Belarussian governments on any income that they earn from U.S. securities, financial instruments held by those governments in the conduct of their financial or monetary policy, or on deposits at U.S. banks.[117] This income is currently excluded from U.S. tax as long as it is not connected to commercial operations of the state in the United States.[118]

I.R.C. § 952.

113 Discussion Draft § 1(c). The discussion draft also is clearly intended to override any inconsistent treaty obligations. *Id.* at §§ 1(d)(3), 2(a)(2).

114 *See* Suspending Normal Trade Relations with Russia and Belarus Act, Pub. L. No. 117-110, § 4(b) (2022).

115 *Id.* at § 4(b)(1), 4(c)(2)(A)-(C).

116 *Id.* § 4(b)(2).

117 Discussion Draft § 2(a)(1); *see also* I.R.C. § 892 (mentioned in the Discussion Draft related to income of foreign governments).

118 I.R.C. § 892.

The discussion draft also extends the reach of the U.S. income tax to individuals and entities not currently taxed ("tax-sanctioned persons"). Tax-sanctioned persons include those people subject to U.S. sanctions in relation to the invasion of Ukraine, the governments of Russia and Belarus themselves, and any other person identified by the Secretary of the Treasury as "meriting the loss of tax benefits" and who is (1) a current or former participant in the invasion of Ukraine; (2) an entity organized in Russia or Belarus that is not a controlled foreign corporation; (3) an executive or officer of an entity described in (2); or (4) related to, an affiliate of, or in a control relationship with a person described in one of the prior three categories.[119]

Tax-sanctioned persons would be subject to several new inbound tax sanctions. First, tax-sanctioned persons would lose the benefit of the portfolio interest exception, meaning that interest earned on their holdings of U.S. bonds would generally be subject to a 30% withholding tax.[120] Second, such persons would be treated as being engaged in a U.S. trade or business—and thereby become obligated to pay tax on their net income connected to that business and file a tax return—if they trade in stocks, securities, or commodities through a resident broker, commission agent, custodian, or other independent agent.[121] Third, income of tax-sanctioned foreign corporations from international shipping and aircraft operations would become subject to U.S. tax.[122] And fourth, certain tax-sanctioned foreign pension funds that had previously been exempt from tax on U.S. real estate gains would become subject to tax on their real estate dealings and obligated to file a U.S. tax return to report that income.[123]

B. An Assessment of the Proposal

The discussion draft includes outbound tax sanctions, inbound tax sanctions, and an extension of U.S. tax jurisdiction that increases the tax reporting obligations of—and hence the information flow from—foreign persons. We assess each category of provisions below.

119 Discussion Draft § 2(b)(1).

120 Discussion Draft § 2(a)(3).

121 *Id.* at § 2(a)(4).

122 *Id.* at § 2(a)(5).

123 *Id.* at § 2(a)(6).

The addition of Russia and Belarus to the list of Section 901(j) states is perhaps the most natural tax sanction to impose, insofar as it relies on existing tax provisions already designed to advance U.S. foreign policy goals. Doing this prevents U.S. tax dollars from indirectly subsidizing Russia and Belarus by disallowing the foreign tax credit for income taxes paid to those states, and it encourages U.S. companies to divest. There has already been a rush by U.S. businesses to self-sanction and wind down their operations in Russia and Belarus,[124] but this trend could easily reverse itself if public attention to the war wanes. The footprint of U.S. businesses in Russia and Belarus is better controlled by tax incentives that are connected to U.S. foreign policy goals than the potentially unstable or fickle winds of public sentiment.

Being listed as a Section 901(j) state means that a portion of the income earned in Russia or Belarus by foreign corporations controlled by significant U.S. shareholders (those owning at least 10% of the foreign corporation's stock) is subject to current tax in the United States. As discussed above, the punitive aspect of this tax sanction was reduced by changes made to the international tax rules in 2017. Moreover, recent changes to the U.S. corporate income tax made in spring 2022 by the introduction of a corporate minimum tax, as well as global coordination on new tax rules negotiated through the Organization for Economic Co-operation and Development ("OECD"), are likely to further weaken this tax sanction and complicate the effectiveness of the foreign tax credit disallowance in ways that are hard to predict. We discuss these developments in more detail in Part V.

On the procedure for removing Russia and Belarus from the list of Section 901(j) states, recall that the President has the authority to do this after consulting Congress and making certain certifications that normalize trade relations under the Trade Suspension Act.[125] By piggybacking on the termination rules under the Trade Suspension Act, the outbound tax sanctions regime will turn off when the higher tariffs imposed under that law are turned off. We think it is wise for the Ways and Means and Senate Finance

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124 Daniel Flatley, Nick Wadhams & Saleha Mohsin, *Corporate "Self-Sanctioning" of Russia Has US Fearing Economic Blowback*, BLOOMBERG (June 14, 2022), https://www.bloomberg.com/news/articles/2022-06-14/corporate-self-sanctioning-of-russia-has-us-fearing-economic-blowback [https://perma.cc/997V-9LWC].

125 Discussion Draft § 1(a).

Committees to be consulted before a certification is made, because they have tax expertise. However, this mechanism means that tariffs and tax sanctions are coupled together, and the President cannot maintain tax sanctions without tariffs or vice versa. There are relatively high barriers to normalizing trade relations with Russia and Belarus, because of the substantive conditions requiring that the Russian withdrawal be acceptable to Ukraine and the congressional procedural requirements and the possibility of a resolution of disapproval. This limits the flexibility of tax sanctions to operate differently from tariffs. We think that it would be preferable to allow for a separate certification process for ending tax sanctions that does not depend on ending trade tariffs.

The discussion draft is remarkable for the creativity and breadth of its inbound tax sanctions. First, inbound tax sanctions would apply not only to persons already subject to U.S. sanctions, but would also include the governments of Russia and Belarus and a person identified by the Treasury Secretary as "meriting the loss of tax benefits" and who either is currently participating in, or has previously participated in, the invasion of Ukraine or which is an entity organized in Russia or Belarus.[126] Also covered by the discussion draft are persons related to such persons or entities.[127] This grant of authority allows the Treasury Secretary to impose inbound tax sanctions on many more foreign targets than might be covered by financial sanctions. Of particular interest should be what—if any—regulatory or other administrative guidance might be necessary, or what justifications the Secretary might offer, in defense of a determination that a person "merits the loss of tax benefits." The discussion draft also grants the Treasury Secretary the authority to impose inbound tax sanctions on parent corporations of Russian or Belarussian subsidiaries located in other states.[128] We worry that imposing tax sanctions in such cases would be viewed by U.S. allies as jurisdictional overreach.

Turning from the scope of affected persons to the substantive inbound tax sanctions themselves, we note first that eliminating the tax exclusion of investment income for Russia and Belarus, subjecting them to U.S. tax on this income, would be a bold step that encroaches on norms of sovereign immunity in international tax

126 Discussion Draft § (2)(b)(1)(C).

127 Discussion Draft § (2)(b)(1)(C)(i)(IV).

128 *Id.*

law. Against the backdrop of the other novel sanctions imposed on the Russian Central Bank this may not seem so remarkable, but it is likely to be a highly salient change for the target governments.

The discussion draft proposes denying the portfolio interest exception to tax-sanctioned persons.[129] Although we think this is a useful tax sanction to have available to foreign policy makers that can reach passive investors in U.S. debt markets who may not be appropriate targets for more severe sanctions, we also think that a more general rule applicable to all outbound investment income payments—including dividends, rents, royalties, and payments on swaps—would be preferable. One reason, recalling our discussion of the advantages of inbound tax sanctions in Part I, is that it may be possible for tax-sanctioned foreign investors to switch into financial contracts that give them similar exposure to U.S. debt. Another reason is the absence of a justification for limiting the tax sanctions to interest payments. In addition to denying the portfolio interest exception, legislation should provide for an adjustable higher rate of tax on outbound passive income payments to tax-sanctioned persons.

Among the more innovative inbound tax sanctions in the discussion draft is the provision that affects not only the income tax liability of tax-sanctioned persons, but also their obligations to file U.S. income tax returns.[130] Foreign persons with a trade or business in the United States must file a U.S. income tax return and pay tax on the income that is effectively connected to that trade or business.[131] Whether activities in the United States rise to the level of being a trade or business is a generally a fact-specific inquiry not defined in the Code.[132] But there is an important safe harbor for foreign persons who hire U.S. investment managers to trade stocks and securities on their behalf.[133] Without this safe harbor, the activities of the manager may be imputed to the foreign investor,

129 Discussion Draft § (2)(a)(3).

130 Discussion Draft § (2)(a)(4) (eliminating securities trading exception for what constitutes a U.S. trade or business).

131 I.R.C. §§ 871(b), 882.

132 Higgins v. Comm'r, 312 U.S. 212, 217 (1941) ("[W]hether the activities of a taxpayer are 'carrying on a trade or business' requires an examination of the facts of each case."); F. Ladson Boyle, *What is a Trade or Business?*, 39 TAX LAW. 737, 738-39 (1986) ("The facts and circumstances test of Higgins is still the basic precept upon which all courts base their decisions.").

133 I.R.C. § 864(b)(2).

making them U.S. taxpayers.[134] By eliminating this exception, tax-sanctioned foreign investors who continue to work with U.S. investment managers would become subject not only to net U.S. income tax rather than U.S. withholding taxes—treatment that might, in fact, lower their tax liability—but more importantly would become obligated to file a tax return and make the required information disclosures under penalty of perjury.

The inbound tax sanctions on foreign shippers and aircraft operators as well as foreign pension funds would also bring these actors within U.S. tax jurisdiction. Whereas our prior article identified the benefits of increasing the effective tax rate and increasing information reporting obligations on *current* U.S. taxpayers,[135] the discussion draft extends U.S. tax jurisdiction in ways that we did not contemplate in our earlier work. These sanctions subject some tax-sanctioned persons to income tax for the first time and impose on them a tax return filing obligation that could be a source of additional information that is useful for foreign policy purposes.[136]

V. Other Developments

The dramatic international economic response to the Russian invasion has, we think, increased the likelihood that tax sanctions will become a fixture of the foreign policy landscape in the not-too-distant future. And the appearance of proposed tax sanctions legislation this past summer leaves us even more bullish. Not only do sanctions such as the freezing of Russian Central Bank assets and the imposition of an adjustable oil price cap reflect a broader imagination for the forms of sanctions, but the institutional capacity that states have had to develop to implement these novel sanctions may make it easier to impose tax sanctions as well. For example, the use of an oil price cap rather than an outright prohibition on Russian oil exports requires economic expertise to analyze the optimal price cap. The Treasury Department is currently recruiting

134 I.R.C. § 864(c). *See also* David S. Miller & Shlomo Boehm, *New Developments in the Federal Income Tax Treatment of CDSs*, 7 J. TAX'N FIN. PRODS. 9, 10 (2009) ("This exemption from federal corporate tax was expressly granted by Congress to encourage foreigners to hire U.S. investment managers for their trading activities and because these trading companies do not compete with U.S. companies.").

135 Deeks & Hayashi, *supra* note 1.

136 The bill also suspends any tax information-sharing agreements between the U.S. and the Russian/Belarussian governments. Discussion Draft § (3)(a).

a sanctions economist to assist with such analyses.[137] And there have been other important developments as well.

On August 16, 2022, President Biden signed into law the Inflation Reduction Act.[138] The Act made a generational investment in tax administration by allocating $80 billion in supplemental funding to the IRS over the next 10 years.[139] These funds are to be used to improve taxpayer services, operations support, and business system modernization, with $45 billion allocated to improved tax law enforcement with a focus on taxpayers with more than $400,000 in taxable income.[140] In most cases, enforcing tax sanctions will require more IRS resources, particularly if those sanctions result in more tax return filings or enhanced information reporting. Thus, we think it propitious that just as the time is right to increase the income tax's role in advancing U.S. foreign policy goals, the IRS is receiving some of the additional resources it may need to support that function.

But not all developments in the last year have been favorable to an expanded tax sanctions regime. There remains a lack of coordination between important developments in U.S. tax policymaking and the foreign policy function. The Inflation Reduction Act[141] itself provides one illustration of this conflict. In the remainder of this Part, we highlight two important U.S. tax law and policy developments that have emerged or become more relevant in the last year. We also briefly discuss recent decisions by the World Trade Organization about the status of the Trump steel and aluminum tariffs, and the implications for using income tax as

137 Wally Adeyemo, *America's New Sanctions Strategy*, FOREIGN AFFS. (Dec. 16, 2022), https://www.foreignaffairs.com/russian-federation/americas-new-sanctions-strategy [https://perma.cc/H7FU-8SNV] ("This new way of deploying sanctions—to segment the market for Russian oil rather than ban it entirely—has required corresponding innovation in analytic methods. Building on this experience, the Treasury Department is currently recruiting a chief sanctions economist who will help develop a full-fledged unit and corresponding analytical capabilities to enhance the United States' ability to undertake this sort of detailed economic analysis in other instances.").

138 Inflation Reduction Act of 2022 (P.L. 117-69).

139 BRENDAN MCDERMOTT, CONG. RES. SERV., IN11977, IRS-RELATED FUNDING IN THE INFLATION REDUCTION ACT 1 (Oct. 20, 2022).

140 Kate Sullivan, *Yellen directs IRS not to use new funding to increase chances of audits of Americans making less than $400,000*, CNN (Aug. 11, 2022), https://www.cnn.com/2022/08/10/politics/yellen-new-irs-funding-audits/index.html [https://perma.cc/T2MB-9S5D].

141 Pub. L. No. 117-169, 136 Stat. 1818 (2022).

a tool of foreign policy in a way that complies with U.S. international obligations.

In addition to making a massive investment in IRS operations, the Inflation Reduction Act introduced a new tax on large corporations known as the Corporate Alternative Minimum Tax (the "CAMT").[142] The CAMT, which applies for tax years beginning after December 31, 2022, applies to corporations with average financial incomes of more than $1 billion and imposes a minimum tax of 15% on the adjusted financial accounting income of those corporations.[143] The tax is designed to ensure that large U.S. corporations cannot reduce their effective global tax rates below 15%. Researchers have found that about 80 publicly traded companies would have owed CAMT in 2021 and the Joint Committee on Taxation estimates that it could affect roughly 150 companies, including Amazon and Ford.[144] Although the IRS recently issued guidance about the CAMT,[145] many details are still unknown, and the tax will make the landscape of international tax planning—already treacherous terrain—even more complicated. Corporations subject to the CAMT must calculate their U.S. liabilities under regular tax accounting rules and then also calculate their liability under adjusted financial accounting rules unique to the CAMT to see if they have any residual U.S. tax liability.

As a general matter, the CAMT will likely undermine the efficacy of outbound tax sanctions much in the same way that the rules introduced in 2017 have done. Before 2018, the active business income of a foreign subsidiary of a U.S. corporation was not subject to current U.S. income tax. Against that backdrop, the tax sanctions that would have applied if the subsidiary earned its income from a Section 901(j) state would cause the income to be taxed at regular corporate rates in the United States—most of which were well in excess of 30% in 2017—and to be subject to an even

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142 *Id.* § 10101.

143 News Release, Internal Revenue Service, Treasury, IRS Issue Interim Guidance on New Corporate Alternative Minimum Tax (Dec. 27, 2022), https://www.irs.gov/newsroom/treasury-irs-issue-interim-guidance-on-new-corporate-alternative-minimum-tax [https://perma.cc/WL9P-YRQM].

144 Jennifer Williams-Alvarez, *Companies Seek Guidance on New U.S. Minimum Tax as Launch Date Nears,* WALL. ST. J. (Oct. 26, 2022, 5:30 AM), https://www.wsj.com/articles/companies-seek-guidance-on-new-u-s-minimum-tax-as-launch-date-nears-11666776601 [https://perma.cc/3KPW-ZU4P].

145 I.R.S. Notice 2023-7, 2023-3 I.R.B. 390.

higher overall effective tax rate because of the tax credit disallowance. In the extreme case that the recognition of income of the foreign subsidiary was deferred indefinitely, the additional tax owed on earning income from a Section 901(j) state could be well in excess of 30 percentage points.[146]

The new rules adopted in 2017 caused the baseline to shift, eliminating deferral and subjecting even active income of foreign subsidiaries to a rate of 10.5%.[147] Moreover, the corporate tax rate is now 21%.[148] Against this new baseline, the punitive effect of earning active income from a Section 901(j) state is only to increase the tax rate by 10.5 percentage points.[149] The CAMT moved the baseline again. For a multinational that has CAMT liability greater than its liability under the ordinary corporate income tax, any increase of its ordinary income tax liability as a result of earning Section 901(j) income (or for any other reason) will have only a muted effect, and in some cases no effect at all, on its bottom line. If the CAMT is to remain a fixture of the U.S. taxation of corporations, then it should be amended so that both the CAMT and the regular corporate income tax increase as a result of earning Section 901(j) income.

The adoption of a new 15% corporate minimum tax in the summer of 2022 occurred amid ongoing global negotiations under the auspices of the OECD to implement a *different* minimum tax of 15% for large multinational corporations.[150] Although the United States has been instrumental in negotiating this global tax deal—of which the minimum tax is "Pillar 2" of a two-pillar structure—from the beginning, there is significant uncertainty about whether the United States will ultimately enact domestic legislation that implements the Pillar 2 minimum tax and how any new law will integrate with both the regular corporate income tax and the

146 This is the difference between current taxation at a rate of a least 30% and the effective rate on income that is deferred indefinitely. If that income is never repatriated, then it is never subject to U.S. tax.

147 The rate will increase to 13.125% in 2026 when the deduction for Global Intangible Low Taxed Income is reduced from 50% to 37.5%. I.R.C. § 250(a)(3)(B).

148 I.R.C. § 11(b).

149 This is the difference between the corporate rate of 21% that is applicable to income from a Section 901(j) state and the rate for GILTI income of 10.5%.

150 Professor Ruth Mason argues that this tax deal has transformed international taxation in dramatic ways. Ruth Mason, *The Transformation of International Tax*, 114 AM. J. INT'L L. 353 (2020).

CAMT.[151]

Perhaps the most important difference between the CAMT and Pillar 2 is that the CAMT imposes a 15% tax on a multinational's global income, whereas Pillar 2 requires a 15% tax rate in each state in which a multinational operates.[152] We can only conjecture how the implementation of Pillar 2 under domestic U.S. tax law would affect outbound tax sanctions, but we would expect that increasing the tax rate on income earned in any state to 15% would generally undermine tax sanctions in a manner similar to the CAMT.[153] What we can say is that any such implementation of Pillar 2 should be done to preserve the efficacy of tax sanctions.

We conclude this Part by noting a recent development that affects the question of whether and how tax sanctions might be imposed in a way that respects the United States' international legal obligations. On December 9, 2022, a panel of the World Trade Organization ruled that steel and aluminum tariffs imposed under the Trump Administration in 2018 violated global non-discrimination trade rules because the exception for measures "taken in time of war or other emergency in international relations" under Article XXI(b)(iii) of the General Agreement on Trade and Tariffs ("GATT") did not apply.[154] The ruling is a repudiation of the position held by the United States and others that the national security exception is "self-judging" and not subject to panel review.[155] One commentator described the ruling as a "shockwave,"

151 Kimberly Clausing, *The Global Minimum Tax Lives On*, FOREIGN AFFS. (Aug. 17, 2022), https://www.foreignaffairs.com/united-states/global-minimum-tax-lives [https://perma.cc/ZMQ7-RC6E] ("[A]lthough U.S. leadership was pivotal in forging this agreement, U.S. lawmakers have come up short."). For a description of the significance of this agreement for international lawmaking, *see* Mason, *supra* note 150.

152 JANE GRAVELLE, CONG. RES. SERV., R47328, THE 15% CORPORATE ALTERNATIVE MINIMUM TAX summary (Jan. 19, 2023) ("The CAMT is different from the 15% Pillar 2 global base erosion (GLoBE) tax proposed by the Organisation for Economic Co-operation and Development and G20 (OECD/G20) and endorsed by 130 countries. The CAMT imposes a minimum tax on worldwide income, whereas GloBE would impose a minimum tax in each country. The tax base is different in numerous ways as well.").

153 There may be aspects of Pillar 2 that would buttress U.S. tax sanctions. For example, an increase in foreign taxes paid will increase demand among U.S. companies for foreign tax credits, which could increase the effectiveness of 901(j) itself in certain cases. We are grateful to Ruth Mason for pointing this out. *See* Mason, *supra* note 150.

154 Doug Palmer, *WTO says Trump's steel tariffs violated global trade rules*, POLITICO (Dec. 9, 2022, 12:58 PM), https://www.politico.com/news/2022/12/09/wto-ruling-trump-tariffs-violate-rules-00073282 [https://perma.cc/G8UX-VNV6].

155 *Id.* ("The United States has held the clear and unequivocal position, for over 70

given the WTO's history of deferring to states about what constitutes a national security threat.[156]

The ruling is relevant because tax sanctions discriminate against the target states and their nationals and may come into tension or conflict with non-discrimination commitments under the GATT.[157] Although in the case of Russia, a panel likely would find that the national security exception permits states to waive Russia's most favored nation status and therefore raise tariffs on Russian goods and services if Russia were to challenge those waivers, it is unclear how the United States will account for the ruling in other cases where applicability of the national security exception is less obvious. The most likely outcome may be that the U.S. position will remain unchanged in the short and medium term. Over the long run, if tension grows between competing interpretations of the exception, and if the United States uses tax sanctions aggressively in cases where there is serious disagreement about whether there is an emergency in international relations or a time of war, the existing challenges to an already weakened GATT framework will worsen.

The Russian invasion does not, however, present such an edge case. One more remarkable development in the implementation of sanctions has been the emergence of a broad international coalition that has co-operated in implementing these sanctions. Although the United Nations is not in a position to mandate global sanctions against Russia on account of Russia's status as a veto-wielding member of the Security Council, multilateral sanctions have emerged outside of that structure. States that have historically been wary of non-UN sanctions, such as Japan, New Zealand, Switzerland, and Singapore, have participated in the Russian sanctions and in doing so are developing enforcement capacity—enabling legislation, resources, and personnel—that could be used again in the future.[158]

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years, that issues of national security cannot be reviewed in WTO dispute settlement and the WTO has no authority to second-guess the ability of a WTO member to respond to a wide-range of threats to its security."). China has brought a case in the WTO alleging that U.S. attempts to block sales of chips to Chinese companies is trade protectionism. The United States has taken its traditional position in response.

156 *Id.*

157 *See* Kathleen Claussen, *Trade's Security Exceptionalism*, 72 STAN. L. REV. 1097, 1102 (2020) (noting that "economic security exceptions have grown in scope and power").

158 Minami Funakoshi, Hugh Lawson & Kannaki Deka, *Tracking Sanctions Against Russia*, REUTERS (July 7, 2022), https://www.reuters.com/graphics/UKRAINE-

Tax sanctions, like most other sanctions, are likely to be more effective when they are imposed multilaterally, because multilateral sanctions provide fewer avenues for evasion. The breadth of the co-operation and development of sanctions infrastructure in other states is encouraging for the future of tax sanctions—at least in cases where there is international support. But the United States need not wait until the next occasion on which it wants to implement tax sanctions to negotiate for co-operation with other states. The OECD and the negotiations around the global tax deal provide a natural forum and context for introducing the possibility of multilateral tax sanctions into the international tax framework. On the one hand, these negotiations are already fraught, and introducing yet another complication may risk derailing them. Moreover, doing this effectively would require consultation foreign ministries and the U.S. Department of State. On the other hand, the global tax deal provides a generational opportunity to create a framework for multilateral tax sanctions.

VI. Conclusion

When we wrote about the need for tax sanctions in January 2022, our primary concern was the need to find alternative points of leverage over foreign targets that would broaden the reach of U.S. sanctions and reduce the pressure being exerted through traditional financial sanctions, which risked divestment from the U.S. financial system and currency over the long term. More generally, we saw the possibility of making more favorable tradeoffs between foreign policy goals and domestic concerns through tax sanctions and through sanctions rules that allowed for finer calibration.

In light of these concerns, developments in sanctions in 2022 were encouraging. The innovation of an adjustable oil price cap as a mechanism for balancing concerns about global energy prices and inflation with the need to reduce Russia oil revenues reflects exactly the kind of calibrated pressure that makes tax sanctions appealing.[159] And as the Treasury Department builds out the capacity to do the economic analysis necessary to maximize the effectiveness of the cap, we hope that the value of this expertise will

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CRISIS/SANCTIONS/byvrjenzmve/ [https://perma.cc/5JLM-7HNG].

159 Press Release, U.S. Dep't of the Treasury, *supra* note 93 ("This price cap is one of the most powerful tools we have to fight inflation and protect workers and businesses in the United States and globally from future price spikes caused by global disruptions.").

become apparent and make tax sanctions—which will require similar economic analysis to be most effective—even more attractive.