

What Contractors Should Know About NY's Russia Sanctions

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As we approach its one-year anniversary, the reverberations of the Russian invasion of Ukraine continue to be felt around the globe.

When Russia invaded Ukraine last year, the international outcry was immediate. Governments throughout the world took steps to isolate Russia economically and diplomatically.

In the U.S., most of the attention has been focused on federal-level trade restrictions and sanctions targeting Russian government assets, broad sectors of the Russian economy, and specific entities and individuals. Escalation of this federal response is expected to continue this year.

But, numerous state and local governments also have adopted regulations and laws aimed at further isolating Russia. New York state in particular took swift action to prevent any support being provided to the Russian government by curtailing the ability of companies that do business with New York state from also doing business in Russia.

While New York's initiative was put in place in the immediate aftermath of the Russian invasion, it required time to implement. Its impact is now being felt as state contracts come up for renewal and bids are solicited for new contracts.

This article summarizes New York's new regulatory scheme, and is instructive for companies that both conduct business in Russia and contract with New York state, or any other state or local government that has imposed similar measures.

New York Executive Orders

New York Gov. Kathy Hochul acted quickly after Russia invaded Ukraine by signing two executive orders aimed at ensuring that New York state was not supporting the Russian government or its war effort.

On Feb. 27, 2022, Hochul issued Executive Order No. 14, which directed state entities to divest from and terminate contracts with businesses headquartered or that have their principal place of business in



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Russia, and to refrain from new investments or contracts with such entities.[1]

The following month, Hochul issued Executive Order No. 16, which had legal and commercial implications, not only for entities based or headquartered in Russia, but also for entities conducting business in Russia.

More specifically, the order:

- Directed state entities to "refrain from entering into any new contract or renewing any existing contract with an entity conducting business operations in Russia";
- Defined an "entity conducting business operations in Russia" as "an institution or company, wherever located, conducting any commercial activity in Russia or transacting business with the Russian Government or with commercial entities headquartered in Russia or with their principal place of business in Russia in the form of contracting, sales, purchasing, investment, or any business partnership"; and
- Permitted the head of a state entity to renew or enter into a new contract with an entity conducting business operations in Russia based on a written determination that the contract is necessary for the state entity to perform its function and no suitable contractual alternative exists.

These two executive orders were far-reaching, going beyond the scope of the Russia-related sanctions implemented by the U.S. Department of the Treasury's Office of Foreign Assets Control.

Given that foreign policy — including Russia sanctions — is an area where Congress generally has intended federal law to occupy the field, the New York executive orders may be vulnerable to a preemption challenge.[2]

Importantly, the federal sanctions regime under OFAC imposes prohibitions on certain broad categories of conduct and on engaging with certain parties, but there is a meaningful subset of Russia-related activities that remains legal under federal law. For example, the provision of certain humanitarian and telecommunications-related goods and services is authorized by OFAC.[3]

These license authorizations represent the federal government's decision that such transactions are consistent with U.S. foreign policy and national security objectives. As described below, while the New York executive orders do not have similar carve outs, New York state will consider mitigating factors in making determinations under the orders.

New York State Guidelines for the Executive Orders

The New York State Office of General Services established guidelines to assist in making determinations under Executive Order No. 16. On their face, the guidelines, like the order itself, put in place prohibitions on commercial ties to Russia that exceed the federal sanctions regime implemented by OFAC.

Save for relatively narrow exceptions, the guidelines effectively bar a vendor that seeks to contract with New York state from engaging in any ongoing business engagement with Russia, regardless of whether

such engagement is prohibited by U.S. sanctions or consistent with U.S. policy objectives including OFAC.

Accordingly, for entities that do or seek to do business with New York state and also engage in business with Russia, the guidelines raise difficult economic and legal questions.

More specifically, the guidelines for certification require state entities to obtain a certification from vendors in connection with new contract bids, contract renewals or the assignment of existing contracts.

The certification requires a vendor to disclose whether it is an "entity conducting business operations in Russia"; and provides four possible responses to be certified under penalty of perjury. The possible responses are:

- Response 1: No.
- Response 2.a: Yes, but the vendor has taken steps to wind down (or is in the process of winding down) business operations in Russia.
- Response 2.b: Yes, but the vendor's business operations in Russia are being conducted only to the extent necessary to provide vital health and safety services within Russia or to comply with federal laws and regulations.
- Response 3: Yes.

A negative responses — Response 1 — allows the procurement to proceed in the usual manner, while an unqualified affirmative response — Response 3 — serves to disqualify the vendor unless, as described below, there are grounds to exempt the vendor from disqualification.

A qualified affirmative response — Response 2.a or Response 2.b — triggers a review by the state entity. If the state entity determines the vendor has made good faith efforts to limit its business operations in Russia and its remaining operations are not contributing in any significant way to the Russian war effort, the contract award can proceed in the usual manner.

If the state entity determines the vendor's remaining operations are contributing to the Russian war effort, the vendor will be disqualified from the contract award, absent a basis to exempt it from the disqualification.

In either case, the state entity's determination must be made in writing.

The guidelines also provide that the head of a state entity may contract with an entity conducting business operations in Russia if the contract is necessary for the state entity to perform its functions and no suitable contractual alternative exists.

Any such exemption must be granted in writing and include a detailed explanation of why the particular vendor is necessary for the state entity to perform its critical functions, and an explanation of why no suitable alternative exists — including what alternatives were considered and why they were not suitable.

Application of the Guidelines to the Executive Orders

The scope of Executive Order No. 16's impact is extensive. It applies to every entity that currently does business or is seeking to do business with any New York state agency. It broadly construes "doing business in Russia" to include not only sales in Russia, but also contracting, purchasing, investing and forming partnerships in that country.

Additionally, while New York state published the guidelines, application of the guidelines to evaluate each vendor's certification is conducted by the individual state entity issuing or renewing a contract, rather than by a single state authority. Further, there is no provision for automatic reciprocity between state entities.

As such, while it seems likely that the determination made by one state entity under the executive order would be followed by other state entities with which a company is seeking to contract, there is no formal mechanism for this coordination.

For many companies, the nature of their business in Russia remains in flux. Long-term partnerships or other arrangements can make divesting or otherwise winding up business relationships in Russia difficult.

Further, in some instances, particularly for services that are provided to the Russian citizenry — as opposed to the Russian military or state apparatus — or that are otherwise consistent with U.S. policy objectives, companies are permitted under federal law to continue their Russian business operations.

As such, in preparing a certification under Executive Order No. 16, a company that continues to have business operations in Russia should be ready to provide the relevant state entity with additional facts about the nature such ongoing business, and to explain how the company has reacted to the Ukrainian-Russian conflict more generally, including with respect to compliance with U.S. sanctions.

As the Russia-Ukraine conflict endures, it is unclear whether the New York's Office of General Services will amend or augment the guidelines applicable to the New York executive orders that seek to prevent companies that conduct business in Russia from doing business with New York state.

In the absence of more extensive guidance, offering a more complete picture of the nature and scope of a company's ongoing business operations in Russia will give the state entity helpful context, and assist in providing a full and fair evaluation of the company's certification submission

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[1] Under EO 14, the term "State Entities" includes New York state agencies and departments and certain public benefit corporations, authorities, boards, and commissions. The Port Authority of New York and New Jersey is not subject to EO 14 or EO 16 (as defined below).

[2] See *Crosby v. National Foreign Trade Council*, 530 U.S. 363 (2000).

[3] https://home.treasury.gov/system/files/126/russia_gl25c.pdf.