Implications of the Confiscation of Russian Sovereign Assets

An Analysis of the Key Economic and Financial Stability-Related Concerns

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April 2025

Executive Summary

Since the first days of Russia's full-scale invasion of Ukraine, when countries immobilized more than $300 billion in Russian sovereign assets, there have been demands to seize the money and use it for the defense against Russian aggression and Ukraine's post-war reconstruction. Some proceeds from the frozen assets are already being employed to back grants and loans to Ukraine under the G7's Extraordinary Revenue Acceleration (ERA) mechanism. But the Trump administration's sudden and dramatic shift away from supporting Ukraine—and the likely need to shoulder a much larger financial burden in Europe—has brought the question of full seizure back to the forefront. While legal arguments have been discussed for some time,[1] economic and financial stability implications have not been addressed in the same comprehensive fashion.

This report addresses the key arguments related to the future role of G7 currencies; the stability of sovereign debt markets and borrowing costs, especially in Europe; the economic precedent set by action vs. inaction; potential retaliation against foreign companies in Russia; and the use of the frozen assets as a bargaining chip in peace negotiations. In recent weeks, the discussion has taken on a further twist as the US appears to be moving away from joint G7 action against Russia and is unlikely to participate in the confiscation of Russian sovereign assets. This disunity creates a set of very different challenges as it pins the US dollar against other G7 currencies, US sovereign debt against European bonds etc. Therefore, we discuss in detail how the impact of asset confiscation could play out for individual countries of the remaining pro-Ukraine coalition.

New geopolitical realities may not leave countries any other choice but to seize the assets—and, while there are costs associated with such a step, they are outweighed by the benefits of providing Ukraine with resources to defend and rebuild itself without G7 taxpayers footing Russia's reparations bill. Inaction, on the other hand, may prove to be enormously costly if Russia were allowed to destabilize peace and prosperity in Europe due to a lack of resources. In addition, a dangerous precedent would be set by Russia being allowed to attack with impunity while its assets overseas are protected.

Our key conclusions are as follows:

1. **The composition of global reserves has not changed despite the immobilization of CBR assets as central banks with large holdings find it extremely challenging to find alternatives.** From the perspective of a central bank, immobilization and seizure have a similar practical effect: the reserves are no longer accessible and cannot be used. More than three years after the initial decision to immobilize more than $300 billion in Russian sovereign assets abroad, there is no evidence for a shift in the composition of global reserve holdings as a result. The reason is simple: divesting from G7 currencies is a major challenge. Fundamentally, central banks require assets that are available at scale, liquid enough, whose value is determined by market forces (i.e., freely floating), and for which hedging instruments are available. These are difficult to find outside of G7 currencies. In fact, the Russian central bank itself undertook a concerted effort to insulate its reserves from additional sanctions after 2014, but found itself with close to half of its reserves in jurisdictions that ended up immobilizing them.
2. **While it is conceivable that certain countries will move away from other G7 currencies and towards the US dollar, it is unlikely for several reasons.** *First*, some important holders of foreign reserves are not on especially friendly terms with the US either, including, most importantly, China. *Second*, countries such as China have deep commercial links to the Eurozone and other G7 countries beyond the US that they

[1] See "Legal Report on Confiscation of Russian State Assets for The Reconstruction of Ukraine," KSE Institute.

may not want to jeopardize by divesting, in particular given the confrontation with the US that is clearly on the horizon. *Third*, decisions about the composition of a country's reserves are largely driven by economic fundamentals and not political decisions, which means that countries that trade extensively with, for instance, the EU, need to hold a meaningful share of their reserves in Euros. *Fourth*, the Trump administration's economic policies—a disastrous trade war, a likely sharp increase in borrowing from already-elevated and potentially unsustainable levels, upside inflation risks, and a potential devaluation of the US dollar—as well as their overall erratic nature means that the US may not be such a safe haven after all in the future. *Fifth*, the political winds in the US may shift rather quickly, and betting solely on the current political power structure does not appear to be a prudent strategy for reserve managers.

3. **Risks to G7 reserve currencies, in particular the Euro, extend beyond those discussed above.** While the confiscation of Russian sovereign assets may come at a certain cost, it is important to recognize that the alternative scenario is not inaction. Rather, it is a situation where G7 countries, especially without the US, may not have sufficient financial resources to support Ukraine's fight against Russian aggression or even their own efforts to protect themselves from Russia's revisionist foreign policy in Europe. Questions surrounding the future role of the Euro become somewhat irrelevant if Russia is not deterred and attempts an invasion of an EU country, at which point the Euro's role and stability would be fundamentally undermined. Other G7 currencies would also be affected should Russia's gross and continued assault on the rules-based international order be successful. Inaction would send a powerful and problematic message to other regimes around the world with territorial ambitions.

4. **Beyond the question of reserve currencies, it is unlikely that countries will succeed in reducing the share of trade settlements in Euros, Pounds Sterling, Yen etc.** These currencies' share is already limited and largely represents trade between or with the countries in question, while settlements without these economies' involvement are relatively unlikely to take place in their currencies. Here, the US dollar is and will remain for the foreseeable future the dominant choice. Therefore, there is little room for a reduction of the Euro's, Pound sterling's and Yen's share as economic actors in these economies are unlikely to agree to the use of different currencies. While Russia has made significant changes to the currency composition of its trade relations moving away from currencies of "unfriendly" countries, the same cannot be said about the global economy as a whole. It is simply not true that the role of the US dollar, Euro etc. in global trade has been fundamentally undermined by measures taken against Russia. The threat of a cryptocurrency like Bitcoin supplanting these currencies is also very minimal.

5. **A key concern relates to markets for sovereign debt and future borrowing costs, but it is far from clear that the confiscation of Russian assets would lead to higher yields—it could do the opposite.** *On the one hand*, seizure could drive up yields for sovereign debt as investors consider investments in confiscating jurisdictions to be riskier and permanently move away from them. In addition, some investors that are worried about the punishment of Russia for its invasion of Ukraine could undertake a temporary attack on certain countries' assets to destabilize markets and send a political message. This would likely involve a country with pre-existing fiscal and debt challenges, which has experienced pressure on its borrowing costs in the recent past. *On the other hand*, it is also possible that confiscation would *reduce* existing upward pressure on European bond yields as borrowing needs to finance the proposed defense buildup and support for Ukraine will be lower to the tune of ~€230 billion.[2] With the majority of investors

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[2] The total value of immobilized Russian sovereign assets (i.e., CBR reserves) is estimated to be around $340 billion (or €310 billion). See "Russia Chartbook," KSE Institute. The number quoted here (of €230 billion) includes all funds held in Euroclear as well as additional

interested in fundamentals and not politically motivated, the positive effect on yields from lower issuance might actually overwhelm the potential and temporary negative effects.

6. **Even if bond yields increased as a result of confiscation, borrowing and debt service costs would be impacted to a manageable degree.** Higher yields would increase the costs of refinancing amortizing debt as well as new borrowing to finance budget deficits, and it would drive up debt service costs for securities issued at flexible interest rates. We believe that the United States, the country with the largest amount of maturing debt and the most significant budget financing needs, is unlikely to be affected as the current administration will not participate in the confiscation of Russian assets. A temporary 50 basis points increase in yields across confiscating countries, excluding the US, would increase debt costs by $37.3 billion, with the largest effects for Japan ($10.0 billion), the United Kingdom ($6.3 billion), and France ($4.9 billion). As far as the deliberate targeting of individual countries is concerned, based on their bond debt-to-GDP ratios and the share of debt securities held by non-residents, France and Belgium are probably the most exposed EU member states, with the non-EU members of the G7 in a less vulnerable position. What this analysis does not take into account is that the US' unsustainable fiscal trajectory, increasingly erratic and inflationary policies, and the threat of dollar devaluation, will likely increase investor interest in other mature debt markets such as those of EU member states.
7. **The ECB has the instruments to deal with a politically-motivated attack on European countries' debt, both in the short as well as medium and long run.** *First*, the Transmission Protection Instrument (TPI) can be used and a politically-motivated attack on one of the EU governments' bonds is exactly the time to deploy it. *Second*, should a longer-term solution be needed, however unlikely, the ECB can move on to use the Outright Monetary Transactions (OMTs) mechanism. The instrument has some disadvantages as it was not designed for external shocks, but rather stability concerns related to a country's macroeconomic outlook, and therefore carries conditionality. On the plus side, there are no limits set on the size of the program. However, we believe that the threat of the ECB to use "whatever it takes" to protect financial stability in the Eurozone should be enough to prevent such an attack in the first place.
8. **While critics of asset confiscation commonly raise the question of precedent, they often neglect the precedent that *inaction* sets.** It is generally accepted that central bank reserves are sacrosanct, and that this is a worthwhile principle because it facilitates international commerce and respects state sovereignty. Thus, in a vacuum, confiscating reserves would risk undermining these key pillars of international cooperation. The choice is not, however, between undermining the sanctity of sovereign assets and doing nothing. Opting not to confiscate sets its own precedent: namely, that a country can wantonly engage in a war of conquest and repatriate its reserves afterwards. It would demonstrate that Russia's reserves abroad enjoy a higher level of protection than key tenets of the rules-based international order, including the inviolability of a country's sovereignty and territorial integrity.
9. **Russia is likely to retaliate by expropriating the assets of foreign companies—but it has already embarked on this course of action, and governments should not socialize the costs of private businesses' decisions with regard to activities in Russia.** Since the start of the full-scale invasion and imposition of sanctions in early 2022, Russia has taken a series of steps to create—and use—a legal framework for the expropriation of foreign companies' assets. While such efforts could be stepped up, the regime will do so whenever it sees fit—whether its assets abroad are confiscated or not. Furthermore,

direct holdings in EU member states and Japan. The remaining immobilized reserves are either located in the US, Singapore, Switzerland, or not accounted for. See "Resolving Accountability Over Russian State Assets," New Lines Institute.

governments should not cover the costs of companies' decisions to do business in a dictatorship by forfeiting ~€230 billion of funds available for protecting Europe and rebuilding Ukraine. Through higher debt issuance and interest rates, taxpayers would be footing the bill for corporations' risky investments.

10. **Should Russia expropriate all remaining assets of companies from "unfriendly" countries, the total amount is estimated to be significantly smaller than the potentially seized CBR reserves.** KSE Institute's Leave-Russia project estimates that total assets of foreign companies that have not exited the Russian market stood at $190 billion at the end of 2023, $131 billion of which belonged to entities from G7 countries.[3] As KSE Institute research also shows that written-off or lost-to-seizure assets by foreign companies—almost all of them from G7 countries—amount to $167 billion, more than half of the potential impact has already materialized.[4] Importantly, a significant share of the remaining amount consists of illiquid assets that are not comparable to central bank reserves in terms of their usability for monetary and fiscal interventions. Furthermore, it is not necessarily in Russia's interest to expropriate these assets on a large scale: the country will need investors to return after the end of the war and indiscriminate retaliatory measures would deter their return, possibly for many years.

11. **Finally, while this argument is not economic in nature, it is important to point out that the confiscation of immobilized Russian sovereign assets does not, in fact, take any bargaining chips off the table when it comes to peace negotiations.** As a third-party countermeasure undertaken by countries on behalf of Ukraine in response to Russia's gross and persistent violations of fundamental principles of international law, confiscation should, preferably, be reversible. In practice, this means that the assets could be returned and counted against Russian reparations for the damages caused to Ukraine. Thus, no matter its ownership, the money remains on the table during negotiations.

The US' turning away from Ukraine and its allies means that other countries, in particular in Europe, will have to carry a much larger burden for their defense against Russian aggression. Confiscating the immobilized Russian sovereign assets would help to pay for it. While concerns surrounding the potential impact of such a step are partially valid, they are ultimately exaggerated. Importantly, they fail to appreciate the dramatic costs of any alternative course of action that does not tap into these funds, as well as the fact that there are policy tools at authorities' disposal to manage any negative impact.

[3] Leave-Russia's public database can be accessed here.
[4] See "Assessing foreign companies' direct losses in Russia: Financial impact, market consequences, and strategic adjustments," KSE Institute.

Concerns Related to the Role of G7 Currencies

Summary of Concerns

Critics of the confiscation of Russian assets often point to the potential consequences for the US dollar, Euro, etc., as the dominant reserve currencies and means of exchange in the global economy. Thanks to the position of their currencies, the United States, Eurozone, and others enjoy the privileges of seigniorage, and, as far as the US is concerned, the capability to enforce wide-reaching sanctions with extraterritorial effects. Should the countries of the G7 confiscate immobilized Russian sovereign assets under their jurisdiction, critics argue, they could weaken their own economic standing by incentivizing a move towards alternative reserve assets[5] and alternative currencies used in international trade.[6] In fact, since the United States and European Union forcibly removed Iran from SWIFT, an important global financial messaging system, in 2012, and since financial sanctions were imposed on Russia in the aftermath of the annexation of Crimea in 2014, rogue states (including Russia) have sought to develop alternatives. In addition, Russia has undertaken a concerted effort to move to alternative currencies for international trade to shield itself from financial sanctions. Through the seizure of a large amount of Russian assets, the G7 could prompt a fracturing of the world's financial infrastructure, thereby threatening the importance of their own economies and financial institutions.[7] With the Trump administration rapidly moving away from its transatlantic commitments, this argument has taken on a different twist: What will be the impact if countries such as China move away from the Euro, Pound sterling, Yen, etc., for reserves and trade settlements, while strengthening their reliance on the US dollar?

Box 1. Reserve Allocation and Currencies in International Trade

Central banks hold reserves for a wide range of reasons related to maintaining economic and financial stability. Whether in the form of foreign currencies or gold, reserves help facilitate payments for imports and service external debts, allow for interventions to keep a domestic currency's exchange rate stable, and provide liquidity in crises. **Most often, reserves are held not in cash but in debt securities** such that they earn interest while remaining liquid enough to be used on demand. **Countries with the largest amounts of foreign reserves tend to be—but are not always—those with large current account surpluses**. China holds, by far, the largest reserves, standing at around $3.5 trillion in February 2025.[8] **Central banks determine the currency allocation of their reserves with three goals in mind: safety, liquidity, and returns.** Thus, the currency denomination of a country's debts and imports are the most important factors at play.

In any transaction in international trade, payment can be settled in one of three currencies: the importer's domestic currency, the exporter's domestic currency, or in a third currency (i.e., a 'vehicle' currency). Vehicle currencies are used for their stability, liquidity, and convenience. They protect businesses from exchange rate risks, are widely available to exchange with most currencies, and are so commonly used that they operate as the financial world's lingua franca. **The world's dominant vehicle currency is the US dollar**: in December 2024, 82% of all trade finance through SWIFT used it; the Euro occupied a distant second place (6.5%). These shares have been quite stable over time.

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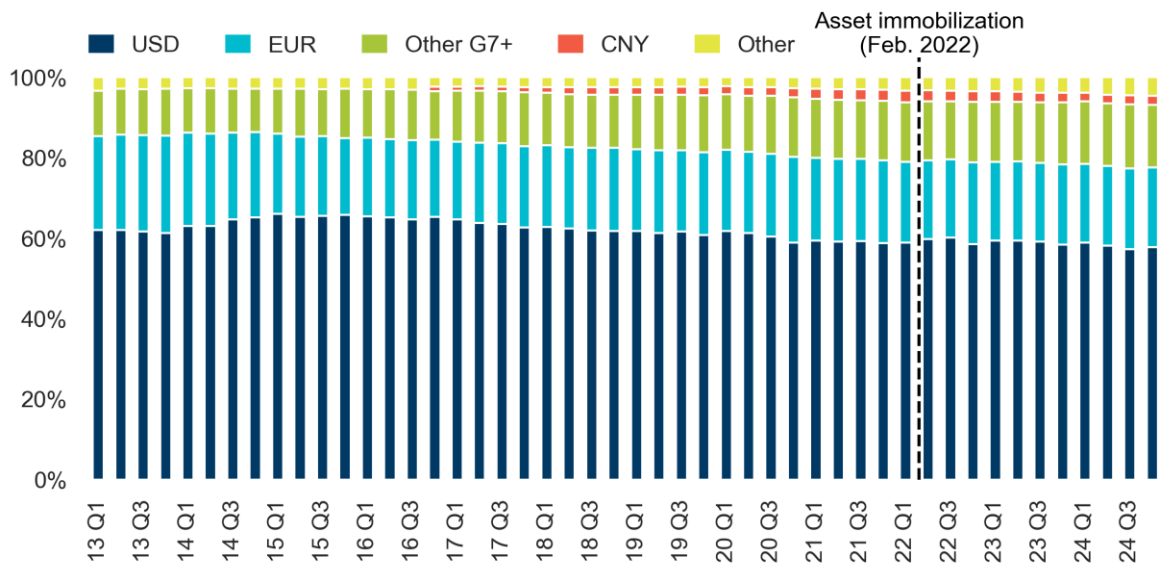
[5] See "The European Union should do better than confiscate Russia's reserve money," Bruegel.
[6] See "The unintended consequences of seizing Russian assets," Foreign Policy.
[7] See "Seizing Russian Assets Isn't as Easy as It Sounds," Foreign Policy.
[8] See "Official reserve assets" from China's State Administration of Foreign Exchange here; "International Reserves and Foreign Currency Liquidity," IMF (accessed on March 24, 2025).

Counterargument: Shifting Reserves Away from G7 Currencies is a Major Challenge

Immobilization of the Russian central bank's reserves has not led to a change in the composition of global reserves. Central banks hold foreign reserves for a number of reasons, including maintaining liquidity for trade, paying sovereign debt liabilities, and serving as a lender of last resort. Global reserves are held predominantly in US dollars thanks to the dollar's stability and central role in global trade, but the currency composition of a given country's foreign reserves also depends on its top trading partners and geopolitics. The question of whether countries with large reserve holdings would attempt to move away from G7 currencies in response to the possible confiscation of CBR reserves is not a theoretical one. This is because, from the perspective of a central bank, the practical implications of immobilization and seizure are very similar—while the legal implications are, of course, very different. Fundamentally, both immobilization and seizure mean that the bank does not have access to its assets. Therefore, it is possible to observe the response of large reserve holders, i.e., current account surplus countries, over a period of more than three years since the assets of the CBR were initially frozen in the immediate aftermath of Russia's full-scale invasion of Ukraine.

The International Monetary Fund's statistics on global reserve holdings[9] reveal that no meaningful shift away from G7+ currencies has taken place since early 2022. In concrete terms, currencies of G7+ countries—the Euro, US dollar, Pound sterling, Japanese yen, Canadian dollar, Australian dollar, and Swiss franc—made up 93.7% of allocated global reserves in 2024 (see Figure 1). This is essentially unchanged from Q2 2021 (94.1%) and only a minor decline compared to the 2017-21 average (95.6%). There has also been little movement within the group of G7+ currencies (see Figure 2). A look at longer-term trends shows that the US dollar's declining share is part of a development that began in 2015-16, when it had accounted for two-thirds of global reserve assets. Importantly, however, the lower share is not a result of any disinvestment from US dollar assets. Rather, global reserves for which the currency composition is known have grown faster than those in US dollars. Reserves denominated in G7+ currencies have, in fact, grown significantly—by 66%, with US dollar reserves increasing by 48%.

Figure 1: Currency composition of global reserve assets, in %

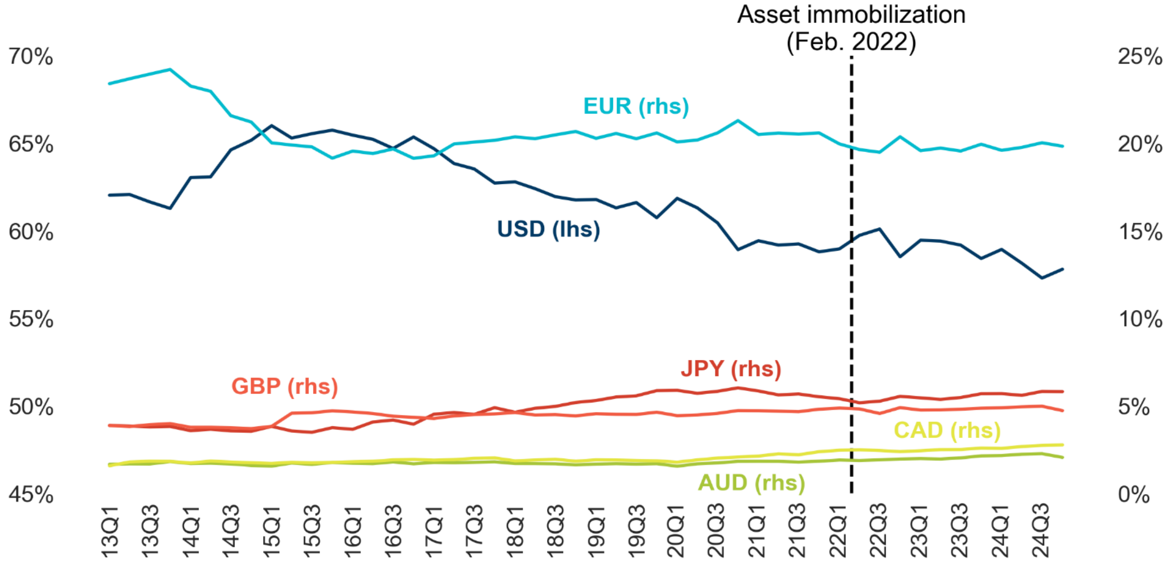


Source: International Monetary Fund, KSE Institute

CNY = Chinese Renminbi, Other G7+ = Australian dollar, Canadian dollar, Japanese yen, Pound sterling, Swiss franc
'Other' includes CNY until Q4 2016

[9] See "Currency composition of official foreign exchange reserves (COFER)," IMF.

Figure 2: G7+ currencies in global reserve assets, in %



Source: International Monetary Fund, KSE Institute

AUD =Australian dollar, CAD = Canadian dollar, EUR = Euro, GBP = Pound sterling, JPY = Japanese yen, USD = US dollar

Two aspects may distort results: unallocated reserves and holdings of gold. On the first topic, assets for which the currency is unknown made up a large share of the global total until around 2016, when it started to decline significantly. Since late 2016, their share has been stable at around 6-7%. Thus, these assets do not meaningfully change the results presented above. Including them leads to a G7+ currency share of 86.8% in 2024 (avg.) vs. 87.7% in Q4 2021 and 87.3% in 2017-21 (avg.). On the matter of gold, its global reserve holdings have increased by under 2% in volume terms between Q4 2021 and Q3 2024, according to the IMF and the World Gold Council.[10] China, Türkiye, Poland, and India saw the largest increases in gold holdings, with China alone accounting for over half of the global increase. There has not been a systematic change in gold holdings across countries. Fundamentally, gold poses several key challenges for central bank reserve managers: it is a finite resource that cannot be employed without serious constraints, it is subject to significant valuation changes, and the holder forgoes liquid investment earnings compared to the holding of other asset classes such as government bonds. The share of gold in global reserves has risen quite sharply in value terms—from 11.9% in 2017-21 (avg.) and 12.9% in Q4 2021 to 18.2% in Q3 2024—but this is largely a result of soaring gold prices, which stood at ~$50,000/kg in 2017-21 (avg.), ~$58,000 in Q4 2021, and ~$85,000 in Q3 2024.

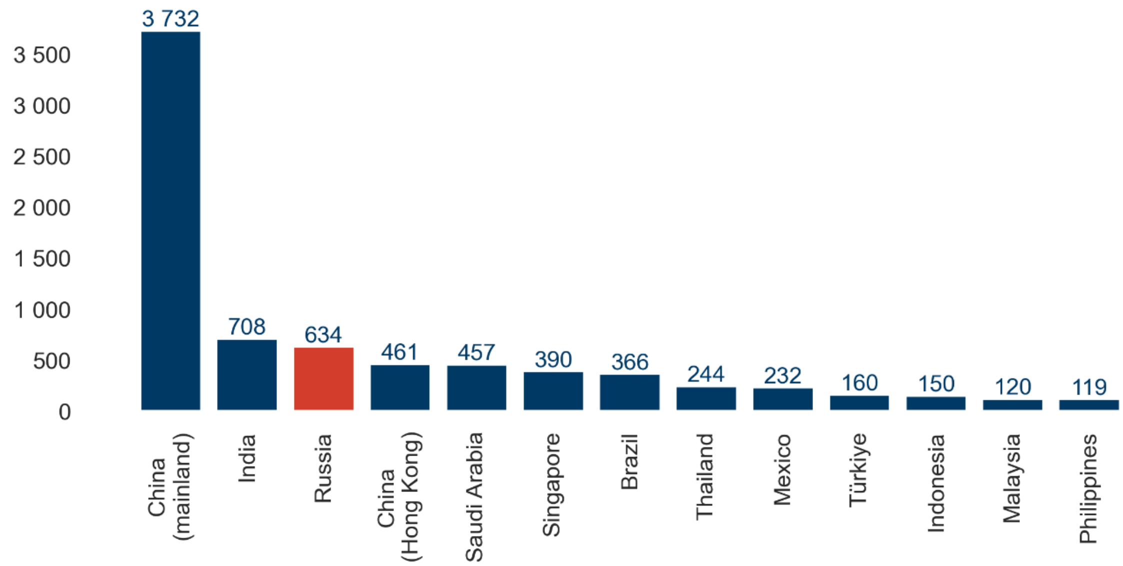
It is very difficult for central banks with large reserve holdings to move away from G7 currencies. The aforementioned findings with regard to the composition of global reserve assets—that nothing has fundamentally changed since the immobilization of the CBR's assets—is not surprising. Fundamentally, modern central banks require assets that are available at scale, liquid enough, whose value is determined by market forces (i.e., freely floating) without capital controls, and for which hedging instruments are available.[11] A look at the emerging markets with the largest reserves illustrates the magnitude of the challenge (see Figure 3). China is the country with the largest reserves, by far: almost $4.2 trillion including Hong Kong. Also notable are India ($708 billion), Russia ($634 billion), Saudi Arabia ($457 billion), as well as Singapore, Brazil, Thailand, Mexico, Türkiye,

[10] Data on gold reserves were drawn from the World Gold Council's database.

[11] Note that despite the immobilization of Russia's reserves, members of BRICS Plus continued to buy euro-denominated debt securities. See "The international role of the euro," ECB.

Indonesia, Malaysia, and the Philippines. It is important to emphasize that, in addition to the challenge of finding assets to put such large amounts of money into, any divestment will inevitably affect the value of one's remaining holdings. This would especially be the case if such a step were intended as retaliation for the confiscation of Russian sovereign assets, i.e., designed to undermine the confidence in certain currencies.

Figure 4: Q3 2024 Reserve assets of non-G7+ countries, in $ billion



Source: International Monetary Fund, KSE Institute

G7+ includes Australia, Canada, European Union member states, Japan, Switzerland, United Kingdom, United States

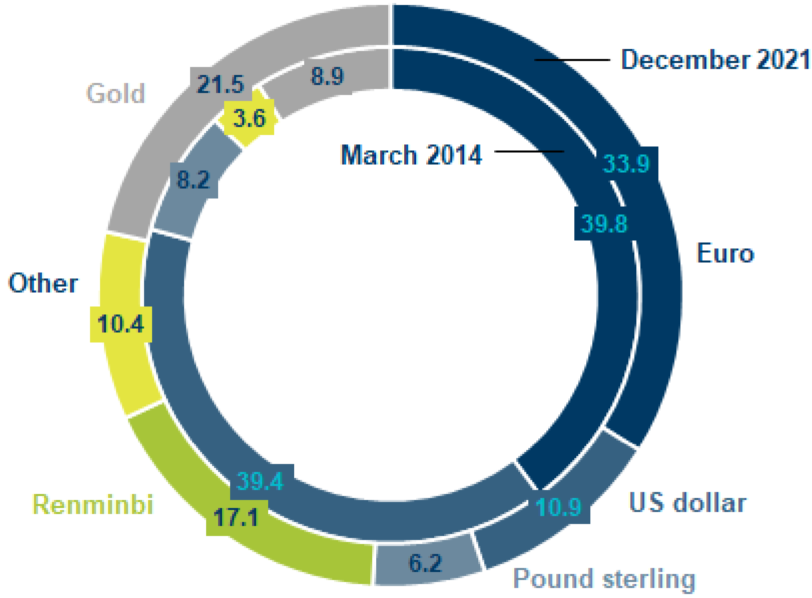
The CBR did not manage to shield its *own* reserves despite a concerted effort since 2014. Central banks have attempted to shield their reserves from sanctions by divesting from G7 currency-denominated assets long before 2022. It was, in fact, the Central Bank of Russia that undertook the most serious effort to do so after 2014. Its efforts, tellingly, proved largely unsuccessful.[12] At first glance, it appears that the CBR managed to significantly reduce its holdings of G7 currency-denominated assets between 2014, when Russia annexed Crimea and faced new Western sanctions, and its full-scale invasion of Ukraine in early 2022. The combined share of Euro, US dollar, and Pound sterling assets declined from 87.4% in March 2014 to 51.0% in December 2021, while the share of Renminbi-denominated assets rose from zero to 17.1% and that of gold from 8.9% to 21.5%. (see Figure 4).

However, this shift coincided with an overall increase in reserves of nearly 30%—from $486 billion to $631 billion. Looking at absolute numbers, we see that the CBR's only true divestment was from US dollar assets. While these assets did drop by nearly two thirds, Pound sterling assets declined by a meager 2% and Euro assets *increased* by 10% (see Figure 5). Thus, when Ukraine's allies banned transactions with the CBR in late-February 2022, thereby freezing its reserves under their jurisdictions, the bank found itself with more than $300 billion in assets that fell victim to these restrictions. The CBR itself, in the face of serious criticism of its preparatory measures, explained that, to maintain a key purpose of reserve assets as a buffer in the case of financial crises, it had not been able to shift a larger share into gold and Yuan assets.[13] Fundamentally, the bank had to balance different types of risks: financial and geopolitical. These are exactly the types of constraints that any central bank attempting to move away from G7 currencies and assets would face, as we outline above.

[12] Nor did the efforts discernibly affect the value of the dollar. See "The other counteroffensive to save Ukraine," Foreign Affairs.

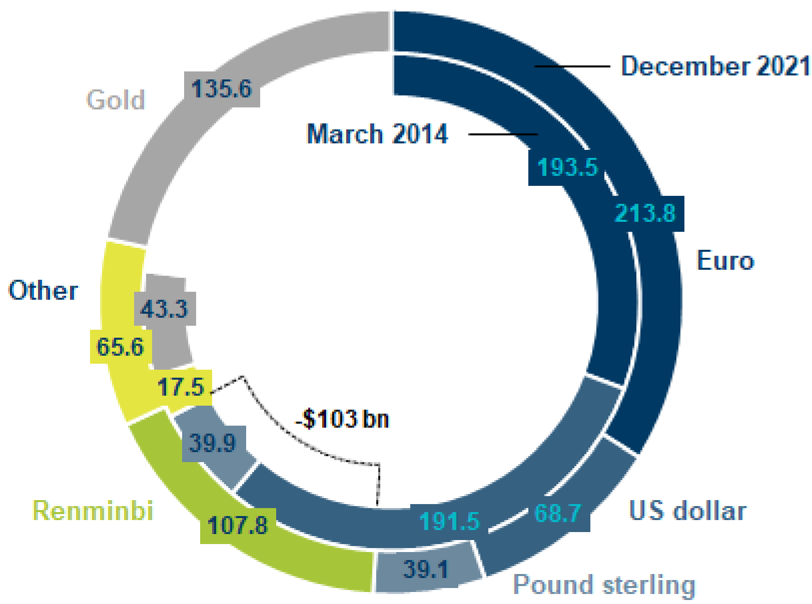
[13] See *Почему Банк России не хранил золотовалютные резервы внутри страны?* under *Золотовалютные резервы* here [ru].

Figure 4: Composition of CBR reserves, in % of total



Source: Bank of Russia, KSE Institute

Figure 5: Composition of CBR reserves, in $ billion



Source: Bank of Russia, KSE Institute

It is theoretically conceivable that countries outside of the G7 will move away from the Euro, Pound sterling, Yen etc., while relying on the US dollar as a safe haven under an administration friendly to their interests. However, there are several practical challenges with such an approach. Some of them are related to geopolitical and geoeconomic realities: *First*, some important holders of foreign reserves are not on especially friendly terms with the US either, including, most importantly, China. It is hard to imagine that Chinese authorities would increase their exposure to the US dollar given that they perceive the United States as their most important geopolitical adversary and are now facing an administration that appears to be focused on a very confrontational approach.[14] The Trump administration's trade war, and the tit for tat response from China, is but the latest example of how the rivalry between the world's two largest economies is being ratcheted up to new levels. *Second*, countries such as China have deep commercial links to the Eurozone and other G7 countries beyond the US that they may not want to jeopardize by divesting, in particular given the confrontation with the US that is clearly on the horizon.[15] *Third*, as mentioned above, decisions about the composition of a country's reserves are largely driven by economic fundamentals and not political decisions. For instance, as the EU accounts for 14.4% of China's exports and 10.4% of its imports, while the corresponding numbers for the US are only 14.7% and 6.3% (all numbers for 2024),[16] holding a meaningful portion of its reserves in Euro is simply a prudent position.[17]

Other challenges are related to the political environment in the US: *First*, the Trump administration's economic policies, including a likely sharp increase in borrowing from already elevated and potentially unsustainable levels and upside inflation risks, as well as their overall erratic nature means that the US dollar may not be such a safe investment after all.[18] In addition, there are reports that the Trump administration will deliberately devalue the dollar, a plan that is fraught with contradictions and outright hostility towards the US' creditors.[19] Central bank reserve managers are generally quite conservative in their investment decisions, which means that significantly higher exposures to US dollar-denominated assets is too-risky a proposition. Just three months into the second Trump administration, a weakened dollar already has investors rethinking the credibility of the US' assets, debt, and currency.[20] *Second*, the political winds in the US may shift rather quickly. It is entirely possible that the current US administration will have no majorities in Congress anymore after the 2026 midterms. In addition, Donald Trump's presidency will inevitably come to an end in early 2029—and the US' policy towards its allies could shift fundamentally once again. Betting solely on the current political power structure does not appear to be a prudent strategy for reserve managers around the world.

Counterargument: Currencies in Trade Are Determined by Fundamental Factors

Russia has undertaken a concerted effort to move away from G7+ currencies in its external trade. According to statistics published by the CBR, the share of currencies of "unfriendly countries"[21] in the settlement of Russian exports and imports of goods and services has fallen dramatically since the start of the full-scale invasion of Ukraine and imposition of sanctions. For exports, it fell from 85% in 2021 (avg.) to 19% in 2024 (avg.) and for imports from 68% to 22%, respectively (see Figure 6). At the same time, the ruble's share rose—from 14% to 41% for exports and from 28% to 43% for imports—as did the share of other currencies—from 1% to

[14] See "Trump shock pushes US and China toward decoupling cliff edge," Bloomberg; "China's central bank asks state lenders to reduce dollar purchases, sources say," Reuters.

[15] As China embarks on its de-dollarization, its only real alternatives are the Euro and the Yen. If China is truly on a collision course with the US, restricting itself even *further* by divesting from the Euro would hardly be feasible. See "China's dollar dilemma," Carnegie. Of the 50% of China's external debt that is denominated in foreign currency, only 8% is in Euros (compared to 80% in US dollars), meaning that there is also little room to reduce their holdings of EU assets. See "SAFE releases China's external debt data at the end of September 2024," Chinese State Administration of Foreign Exchange.

[16] See China's General Administration of Customs' data for 2024 here.

[17] The same logic applies to the emerging markets in which China has stoked fears of the West imposing Russia-like sanctions wantonly on unfriendly regimes. See Zongyuan Zoe Liu's testimony before the US-China Economic and Security Review Commission. It will be crucial for G7 countries to convey the legality of their decision to the rest of the world and not to cede the information space to Russian and Chinese dominance.

[18] See "As Trump sinks dollar, once-unthinkable worry grips markets," Bloomberg; "Treasuries selloff ramps up as investors spurn US long-end bonds," Bloomberg; "US treasuries sell-off deepens as 'safe haven' status challenged," Financial Times.

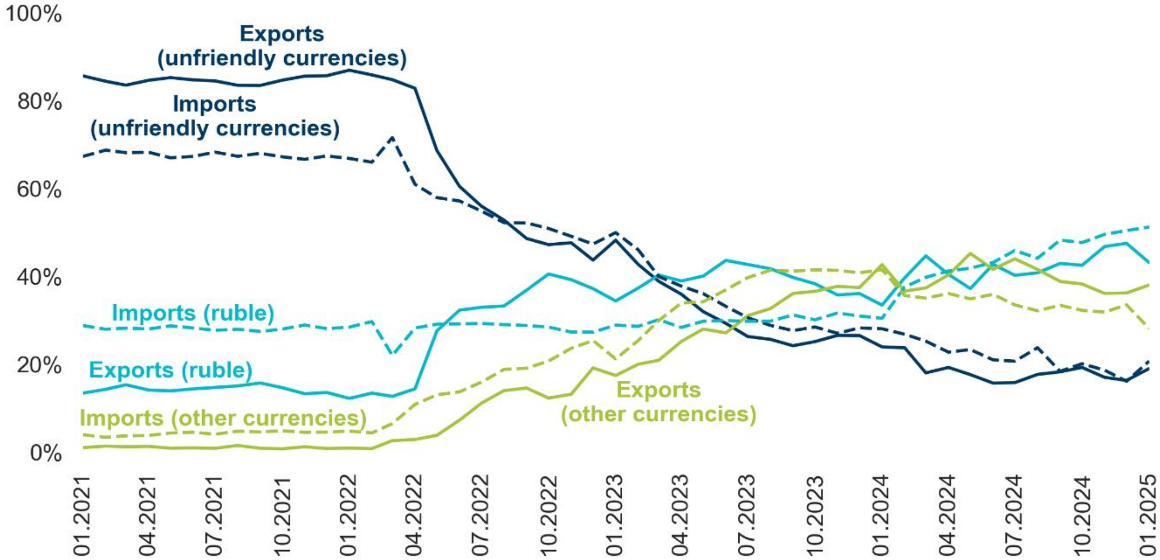
[19] See "Is Trump engineering the decline and fall of the dollar," by Jeffrey Frankel in Project Syndicate; "Could Trump drive down the dollar?" BNP Paribas.

[20] See "Trump's trade whiplash sends dollar into tailspin," Yahoo Finance; "Are the US dollar's days of dominance numbered?" Bloomberg.

[21] The Russian government's directive No. 430-r on March 5, 2022, lists 48 "foreign states and territories involved in unfriendly activity towards Russia, Russian companies and citizens", including Australia, Canada, member states of the European Union, Japan, Singapore, Switzerland, the United Kingdom, and the United States, and, thus, all countries that have immobilized Russian sovereign assets under their respective jurisdiction and may confiscate them. See here.

40% for exports and from 4% to 35% for imports. While the CBR data does not break down these currencies, prior reports by the central bank show that “unfriendly” currencies are essentially US dollars and Euros, while the “other” category consists of Yuan.[22] It is also known from media reporting that trade between Russia and China, where some of the most concerted efforts to change the currencies of trade settlements were made, is increasingly conducted in Yuan and rubles.[23] While this has been possible in the case of trade relationships that are essentially balanced—when exports and imports have broadly the same value—such as the one between Russia and China, it has proven to be much more difficult otherwise, e.g., in the case of Russia and India where exports are much larger than imports.[24] Fundamentally, alternative currencies can often not easily be exchanged at scale and Russian banks and companies may end up with large amounts in overseas accounts that cannot be used as flexibly as intended.[25] This is precisely the dynamic that incentivizes the use of ‘vehicle’ currencies—the US dollar and the Euro—for transactions that do not otherwise involve the US or Eurozone.

Figure 6: Currency composition[26] of Russia’s trade in goods and services, in %



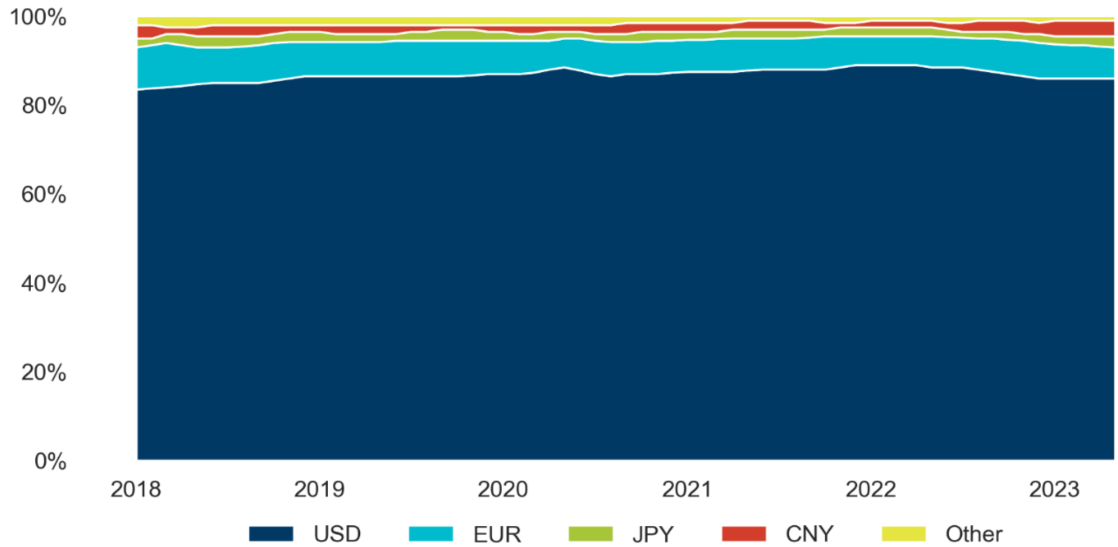
Source: Bank of Russia, KSE Institute

The shift away from G7 currencies in the settlement of global trade has been gradual at best. While data on the use of currencies in international trade comes with a significant lag, we have information for a sufficiently long period after February 2022 to derive some conclusions. In 2021, the US dollar, Euro, and Yen accounted for over 90% of trade finance covered by SWIFT, while the Yuan accounted for around 2%. In December 2024, the shares were 82% (USD), 6.5% (EUR), 1.4% (JPY), and 6% (CNY), capping off a year that saw a slight decline in the US dollar (see recent trends in Figure 7). Thus, we do not see a significant impact from the sanctions imposed on Russia, including the immobilization of the CBR’s assets abroad, at least as far as transactions through SWIFT are concerned. Of course, countries such as Russia and China have also moved away from SWIFT, which means that

[22] According to Russia, almost 90% of the trade between Russia and China is now settled in Yuan or Rubles. See here. For a breakdown of ‘unfriendly’ and ‘friendly’ currencies, see the CBR’s overview of financial markets risk from June 2023 here [ru].
[23] See “What are the limits to Russia’s ‘yuanization’?” Carnegie, and here.
[24] See “India pushes rupee deals as Russia trade rises fivefold,” Bloomberg.
[25] See “Exclusive: Russia payment hurdles with China partners intensified in August,” Reuters.
[26] Governmental Decree No.430-p of March 5, 2022 approving the list of “unfriendly” states, see here. The list of unfriendly jurisdictions includes more than 50 states and territories, including the United States, all EU member states, Ukraine, the United Kingdom (including all British Overseas Territories and Crown Dependencies), Australia, Canada, Norway and Switzerland.

the shift away from G7 currencies is possibly understated.[27] Nevertheless, it is simply not true that the role of the US dollar, Euro etc. in global trade has been fundamentally undermined by measures taken against Russia in response to its full-scale invasion of Ukraine.[28] The IMF states that the continued dominance by these currencies, especially the US dollar, is related to the fact that much of commodity trade continues to be invoiced and settled in dollars.[29] Given the US' current foreign policy stance, there appears to be little incentive for this to change in the foreseeable future; nor are other currencies, notably the Yuan, viable alternatives to the petrodollar. The Yuan lacks the liquidity and accessibility that make the US dollar (and, to a lesser extent, the Euro) attractive. There is also little chance that a cryptocurrency, like Bitcoin, could supplant any of the major currencies used in trade (or in reserves stockpiles,[30] for that matter). It lacks the liquidity and convenience necessary to challenge the dominant fiat currencies, and its price volatility makes it an unreliable means of exchange.[31]

Figure 7: Currency composition of global trade finance



Source: International Monetary Fund, SWIFT, KSE Institute

A reduction of trade invoicing in Euros or other non-US dollar G7+ currencies is unlikely even considering the US' foreign policy shift. Trade settlements in Euro—and Australian dollar, Canadian dollar, Pound sterling, and Yen for that matter—account for a relatively small share of trade finance through SWIFT and largely represent trade between or with these countries, while settlements without these economies' involvement are less likely to take place in their currencies. Therefore, there is little room for a reduction of the Euro's and Yen's share as economic actors are unlikely to agree to different currencies for trade settlements. As far as transactions between countries settled in a third country's currency are concerned, the US dollar is and will

[27] Even transactions made through China's Cross Border Interbank Payment System (CIPS), which serves as an alternative to the US' Clearing House Interbank Payments System, continue to use SWIFT, see: "Sanctions, SWIFT, and China's Cross-Border Interbank Payments System," CSIS. For more discussion of CIPS and the internationalization of the Yuan, see "Internationalization of the Chinese renminbi: progress and outlook," FEDS Notes.
[28] The use of the US dollar and Euro is further incentivized by the international monetary system's strong inertia. See "Currency usage for cross border payments," IMF.
[29] See "Geopolitics and its impact on global trade and the dollar," IMF.
[30] ECB President Christine Lagarde has vocally opposed the use of Bitcoin in the ECB's reserves, arguing that the cryptocurrency is neither liquid, secure, nor safe. See "Lagarde hints at further ECB rate cuts, rules out Bitcoin reserves," Euronews.
[31] See "ETF approval for bitcoin – the naked emperor's new clothes," ECB.

remain for the foreseeable future the dominant choice.[32] This is fundamentally independent of the US' future foreign policy towards its allies and towards Ukraine and Russia.

Moving away from G7+ currencies does not fully insulate actors from sanctions. Invoicing transactions in currencies other than the US dollar, Euro etc. may protect the specific items in question from the reach of sanctions or other restrictive measures; however, as long as the involved institutions conduct *any* business in US dollar, Euro, etc.—which the overwhelming majority do—they remain at risk of facing consequences for their actions contrary to US and European policy. Of course, this is most relevant in the context of US secondary sanctions, which extend the reach of US policy extraterritorially, but access to the European or UK financial systems also provides considerable leverage. In fact, while being fundamentally opposed to extraterritorial measures, these jurisdictions have created instruments in the recent past that allow them to target third-country entities, for instance for their involvement in the evasion and violation of export controls. To fully insulate oneself from sanctions, one must move all of one's business activities away from the currencies and financial systems in question—not a realistic proposition for most globally active companies.

Counterargument: The Future of the Euro is Under Threat if Russia Wins

While the confiscation of Russian sovereign assets may have certain consequences, it is important to recognize that the alternative scenario is not inaction. Rather, it is a situation where G7 countries, especially without the US, may not have sufficient financial resources to support Ukraine's fight against Russian aggression or their own efforts to protect themselves from Russia's revisionist foreign policy in Europe. EU countries still have bad memories of the sovereign debt crisis that started in 2009 when government debt spreads widened and the Euro came under pressure, particularly in 2012 on concerns of Grexit and Italian debt becoming unsustainable. However, imagine if today, Russia were to put pressure on the Baltic states or—worse yet—invade the territory of EU countries. Questions surrounding the future role of the Euro become somewhat irrelevant if one or more countries of the Euro area are attacked and/or occupied by Russia.

Concerns Related to Bond Markets and Borrowing Costs

Summary of Concerns

Of all potential consequences associated with the confiscation of Russian sovereign assets, the most direct costs to G7 governments would come by way of bond markets and debt service costs. Specifically, the decision to seize the CBR's immobilized reserves would change the assessment of risks related to G7 sovereign debt in global markets. This discussion is largely focused on European countries with fiscal and/or debt sustainability concerns. Fundamentally, critics of asset confiscation claim that higher borrowing and debt service costs could offset—or more than offset—the amount of money secured through seizure, while undermining the stability of markets for European and other countries' sovereign debt.[33]

Relatedly, critics of asset confiscation have raised concerns about the €45 billion in loans that G7 countries have provided Ukraine through the ERA initiative, which are backed by future proceeds from immobilized CBR assets

[32] For a more in-depth discussion of dollar dominance amidst trade fragmentation, see "Geopolitics and its impact on global trade and the dollar," IMF. For analysis of longer term trends in currency invoices, see "Patterns in invoicing currency in global trade," IMF.
[33] See "Seizing central bank assets?" Ferrari Minesso et al.; "Confiscating sanctioned Russian state assets should be the last resort," Chatham House; "Russia's frozen assets present a policy dilemma," Carnegie; and "ECB warns Brussels against windfall levy on frozen Russian assets," Financial Times.

and could, thus, be destabilized by their seizure.[34] A simple solution to this matter would be for Ukraine to invest the assets and service the loan with its returns. Ukraine would likely generate higher proceeds by doing so as well since a large share of the CBR's immobilized assets abroad have now matured and turned into cash,[35] meaning they are held in bank accounts, which do not yield high returns.[36]

Box 2. Sovereign Debt Markets and Bond Yields

Government bond yields are primarily influenced by prevailing interest rates and the credit risk of the issuer. When central banks raise monetary policy rates, for instance to curb inflation, bond yields increase as investors demand higher returns to compensate for holding bonds. Conversely, yields fall when central banks cut rates. Additionally, the credit risk of the issuer significantly affects yields; investors require higher yields for bonds from riskier issuers to offset the higher risk of default. Finally, global factors, such as G7 central bank decisions or geopolitical events, can impact bond markets worldwide, creating contagion effects.

Government bonds, especially those issued by highly rated countries like the US and European nations, are considered low-risk investments and serve as benchmarks for pricing corporate bonds in those countries. **These bonds are held by a wide range of investors, including individuals, institutions—domestic and international banks, pension funds, insurance companies, and mutual funds—and foreign governments.** Central banks also hold government bonds as part of their monetary policy strategy, using them to transmit policy rates to broader market and lending rates. Foreign governments and sovereign wealth funds purchase these bonds to diversify reserves or as a safe investment.

Counterargument: The Impact on Borrowing Costs Is Not Clear

Asset seizure could impact markets in more than one way. *On the one hand*, seizure could drive up yields for sovereign debt and negatively impact the value of private sector assets as investors consider investments in seizing jurisdictions as riskier and permanently move away from them. In addition, a small group of investors that are worried about the punishment of Russia for its unprovoked and illegal invasion of Ukraine—e.g., in China, Saudi Arabia[37]—could undertake a temporary attack on certain countries' assets to destabilize markets and send a political message. Given the size and role of its sovereign debt market, as well as the fact that the US is unlikely to participate in the confiscation of CBR assets at this point due to the Trump administration's stance on Ukraine and Russia, the US is an extremely unlikely target for such a strategy. More likely, it would be a country with pre-existing fiscal and debt challenges, which has experienced pressure on its borrowing costs in the recent past. However, most of the investments in European government bonds happen for purely financial risk-reward reasons; they are highly rated assets held for investment opportunities.[38] In addition, the group of more politically motivated asset holders is smaller than the rest of the market.

***On the other hand*, it is also possible that the confiscation of Russian sovereign assets would *reduce* existing upward pressure on European bond yields as borrowing needs will be lower.** With European contributions to Ukraine's defense partially covered by confiscated Russian assets, countries would be able to allocate freed-up budgetary funds to their own proposed defense build-up, and new debt issuance will, in turn, be

[34] See "No return to 'whatever it takes' for EU defence - BdF head," Central Banking; "Seizing Russian Assets Isn't as Easy as It Sounds," Foreign Policy.
[35] See "Resolving Accountability Over Russian State Assets," New Lines Institute.
[36] See "A fresh look at the Russian assets," Hoover Institution; "Mobilizing Russia's immobilized reserves," CFR; "Using the returns of frozen Russian assets to finance the victory of Ukraine," CEPR.
[37] See "Saudis warned G-7 over Russia seizures with debt sale threat," Bloomberg.
[38] See "The world is finding a plausible alternative to treasuries," Bloomberg.

lower. And defense expenditures are only part of the equation. Fundamentally, if Ukraine's allies decide *not* to confiscate the assets, they will still face the question of how to address the cost of Ukraine's post-war reconstruction.[39] As of the end of 2024, the cost of reconstruction and economic recovery was estimated at $524 billion by the World Bank in its fourth Rapid Damage and Needs Assessment (RDNA4).[40] The aforementioned potential negative impact on borrowing costs must therefore be compared not to a "no-action" scenario, but to one where funds are made available in a different fashion—including, to a significant extent, by European countries.

A look at the yields of German sovereign debt following the announcement of significant additional infrastructure spending (of €500 billion over 12 years) and a reform of the country's debt brake, which allows for hundreds of billions in military spending, shows that investors are fundamentally concerned about Europe's fiscal outlook. The yield on the 10-year Bund was up ~20bps on the day of March 5 when the announcement was made and continued to drift up (to ~35bps) in the following days. As German debt functions as a benchmark for other sovereign assets, yields for other countries' debt rose in turn.[41] The impact could be significantly exacerbated—i.e., result in larger spreads—should these countries' yields reach a level that poses questions to fiscal stability and debt sustainability. With the EU planning to allow member state governments to spend €800 billion on defense, hundreds of billions are likely needed in additional issuance.[42] Part of this money will be needed to support Ukraine's defense needs as the US reduces its support. Thus, should the EU decide to seize Russian assets, this would effectively be a grant of ~€230 billion, improving the EU's fiscal position and reducing issuance needs. This will likely be viewed by the markets as overwhelmingly positive and reduce pressure on the yields. With the majority of investors interested in fundamentals and not politically motivated, the positive effect on the yields from lower issuance might actually overwhelm the potential and temporary negative effects.

It is difficult to foresee to what extent bond yields will react—or whether they will do so at all. If one is interested in calculating the negative effect, one has to look at the share that would likely be repriced.

Counterargument: The Actual Cost of Rising Interest Rates Is Limited

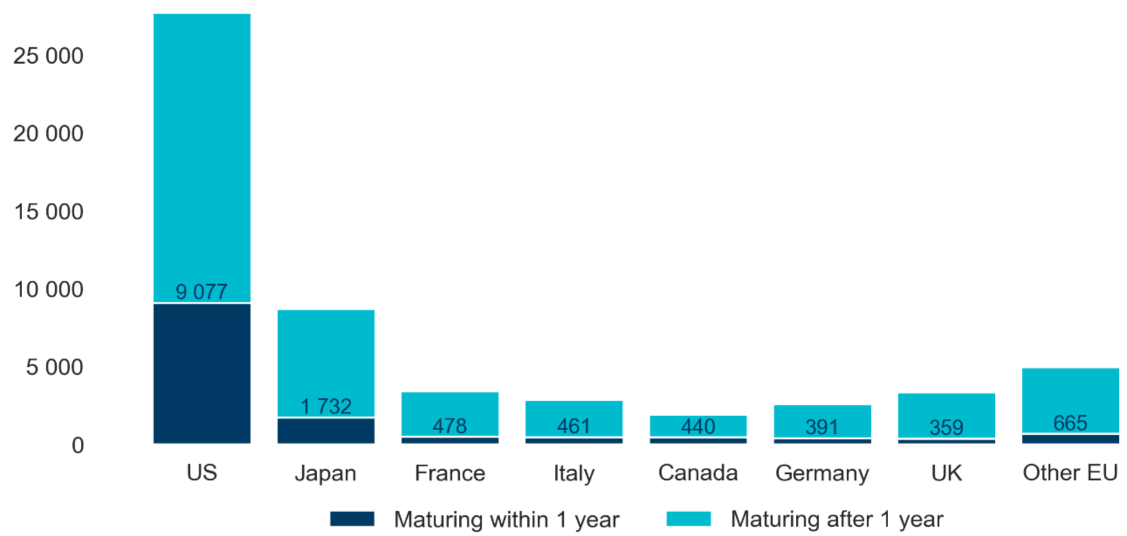
Debt service costs will only rise for the amount that needs to be rolled over within a certain period. Critics of asset confiscation often apply a certain increase in sovereign bond yields to the entire stock of G7 debt, which stands somewhere around $55.4 trillion. Not surprisingly, this leads to significant additional debt service costs that may reach the value of the confiscated CBR assets relatively quickly. However, this is methodologically incorrect. Higher interest rates will only affect: 1) the amount of debt that needs to be rolled over within a certain period of time, 2) debt that is issued at flexible rates, and 3) debt that will need to be issued over this period to finance future budget deficits. Here, it also matters whether the increase in interest rates is permanent or temporary.

Based on data from the BIS, supplemented with information from the US Treasury Department,[43] we find that roughly $13.6 trillion of G7 sovereign debt will mature—and, thus, be rolled over—within one year (see Figure 8). This includes debt with an *original* maturity of less than one year and long-term debt with a *remaining* maturity of less than one year. The total amount of debt to be refinanced within one year is highest for the United States at $9.1 trillion (67% of the total), followed by Japan at $1.7 trillion (13%), France at $478 billion (4%), Italy at $461

[39] Seizing CBR assets is not only the morally right decision, but also likely the only path to funding Ukraine's extensive reconstruction needs. See "Russia and the long shadow of Versailles," Barry Eichengreen in Project Syndicate.
[40] See "Updated Ukraine recovery and reconstruction needs assessment released," World Bank.
[41] Spreads have remained steady in the Eurozone in the month since Berlin's announcement, even as borrowing costs have ticked up, which is a positive sign for stability. See "Germany's spending push drives up borrowing costs across Eurozone," Financial Times.
[42] See "Press statement by President von der Leyen on the defence package," European Commission, and "EU ministers back proposal of temporary exemption on defence spending in EU rules," Reuters.
[43] For the US, we consider only marketable debt held by the public (i.e., we exclude non-marketable and intragovernmental debt holdings), according to the US Treasury's Monthly Statement of the Public Debt released in September 2024.

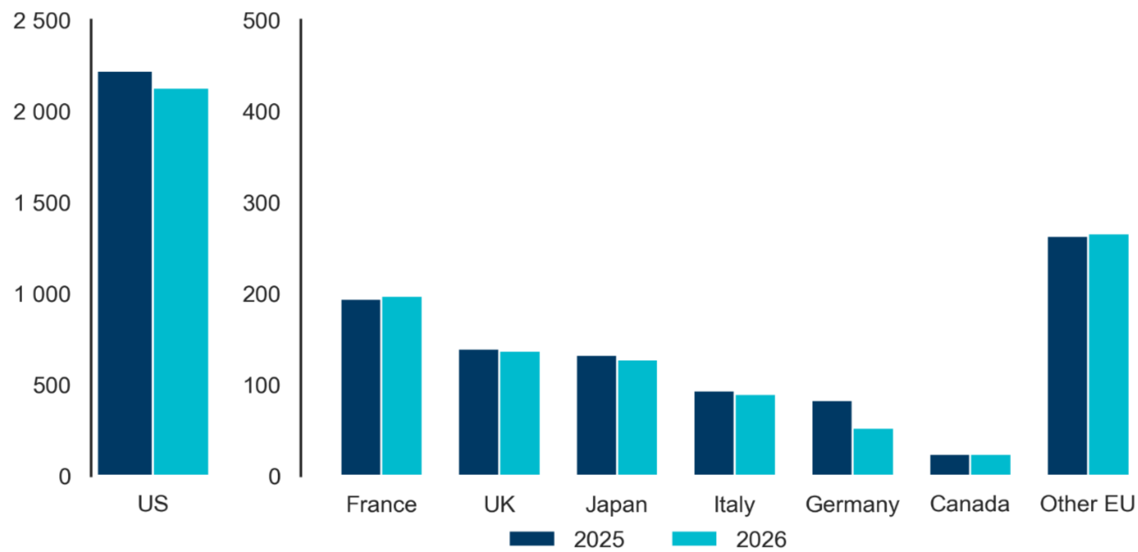
billion (3%), Canada at $440 billion (3%), Germany at $391 billion (3%), and the United Kingdom at $359 billion (3%). For the remaining 24 countries of the European Union,[44] the value is $665 billion (5% of the total). In addition to maturing debt, rising yields will affect debt issued at flexible rates. While the available data—except for the US—does not show the share of such debt by maturity, we can attempt an estimation by applying the overall ratio to the amount maturing outside of 1 year. For the G7 countries, this could mean an additional $2.3 trillion in debt affected by rising rates. The United Kingdom and Italy display the highest shares of debt at flexible rates.

Figure 8: Sovereign bond debt by maturity, in $ billion



Source: BIS, US Department of the Treasury, KSE Institute

Figure 9: G7 general government deficits, in $ billion

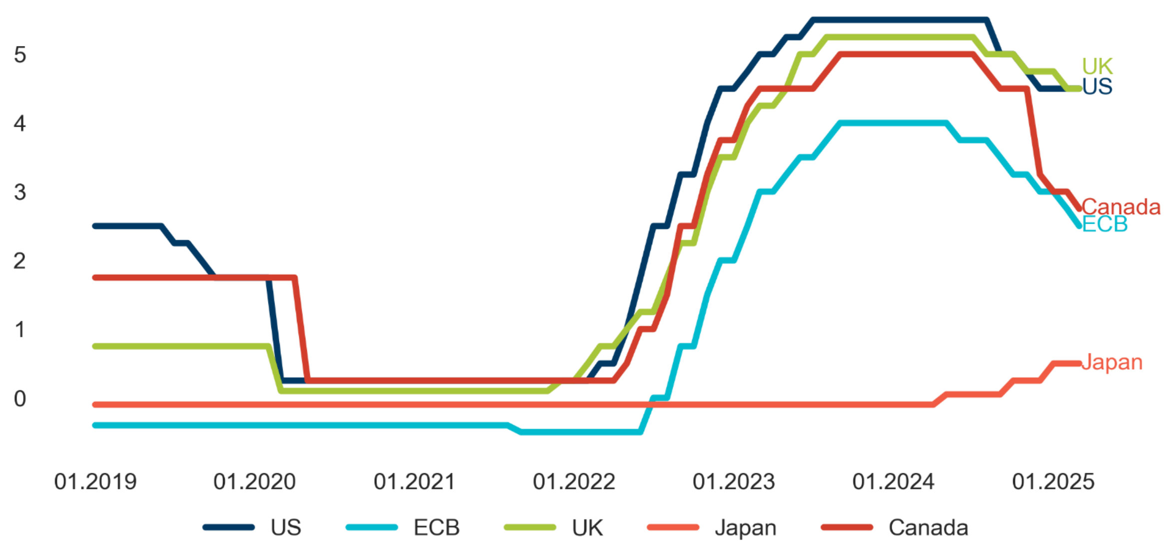


Source: International Monetary Fund, KSE Institute

[44] Romanian debt is excluded, due to its absence from the BIS database.

In addition to the roll-over of maturing debt and servicing of debt at flexible rates, higher interest rates would impact budget financing. According to the IMF's World Economic outlook, G7 countries are expected to record a general government deficit of $3.2 trillion in 2025, with the United States alone accounting for $2.2 trillion (see Figure 9). Other EU member states are forecast to reach $263 billion. These forecasts predate recent decisions by the EU and some member states to increase spending on defense; thus, deficits will likely be significantly higher for the foreseeable future. The same is true for the US, albeit due to the Trump administration's and the Republican Congress' looser fiscal policies. It is also worth noting that all of this would take place in an environment of falling interest rates as all G7 central banks (except for the Bank of Japan) have entered a cutting cycle after post-Covid inflation spikes largely dissipated (see Figure 10). While sovereign bond yields are not the same as policy rates, they tend to follow central banks' monetary policy decisions with a certain lag, i.e., the entire yield curve moves over time. Finally, bond yields fluctuate for many reasons—and have done so for the countries in question in recent months and years (see Figure 11). The extent of additional borrowing, especially by European countries, ultimately depends on whether Russian assets are confiscated or not—to the tune of ~€230 billion.

Figure 10: Policy rates in G7 countries, in %



Source: Bank of Canada, Bank of England, Bank of Japan, ECB, US Federal Reserve, KSE Institute

Targeting of a specific country could be absorbed; yield increases across the G7 would be painful. Taking into account the three channels outlined above—higher costs for the refinancing of maturing debt, higher debt service for debt issued at flexible interest rates, and higher costs for budget deficit financing—we find that a 50 basis points increase in bond yields would trigger total costs of $95.5 billion for all G7 countries within one year (see Figure 12). While this is obviously a very large number, it conceals the varying exposure of different countries. The United States, which is least likely to be affected by any attempts to target its bond market due to the market's size and the global role of US government debt securities, account for $58.2 billion (or 61% of the total), followed by Japan at $10.0 billion and the United Kingdom at $6.3 billion. The three EU countries within the G7—Germany, France, and Italy—together would face additional costs of $12.5 billion over one year. While this is a significant amount, it is entirely manageable and small compared to the overall costs of the response to Russian aggression

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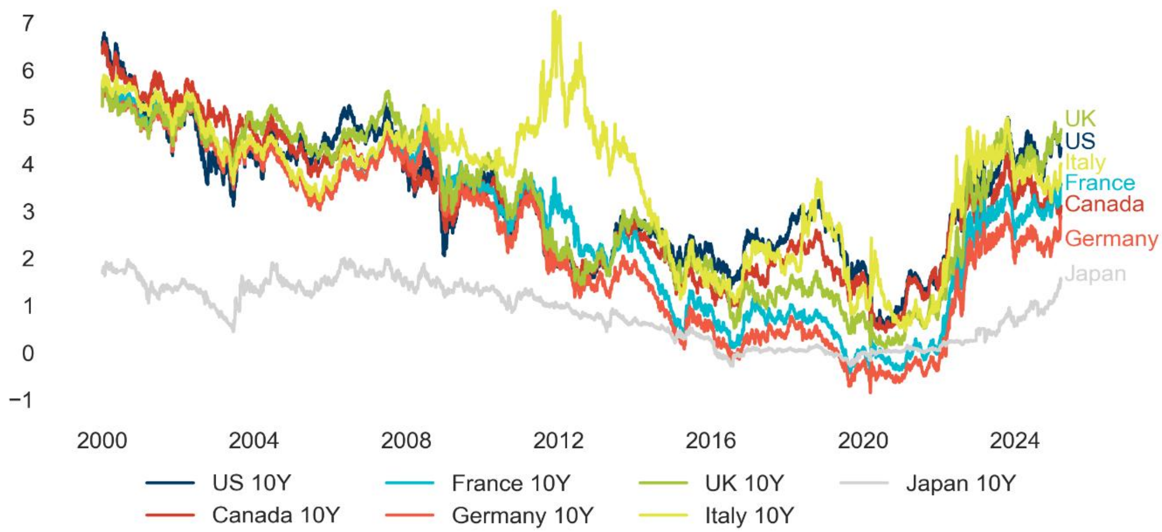
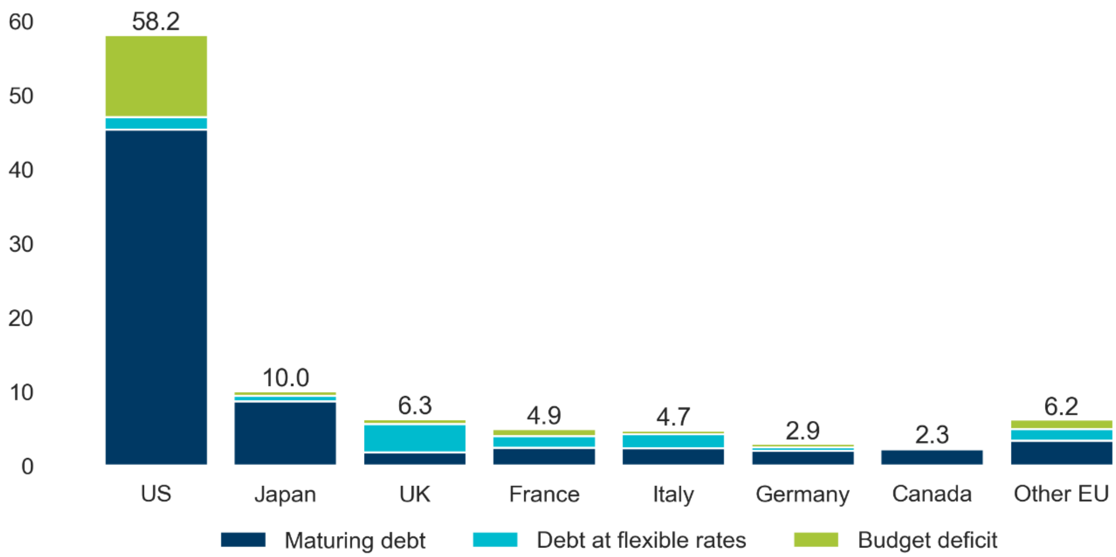
Figure 11: G7 10-year generic bond yields, in %



Source: Bloomberg, KSE Institute

Figure 12: Potential costs of 50 bps rise in yields, in $ billion



Source: KSE Institute

The risks to individual bond markets are unevenly distributed across the G7; France and Belgium are the most vulnerable targets. Even before any instability introduced by the confiscation of Russian assets, the Eurozone is not without risks. But despite geopolitical uncertainties and rising borrowing costs, markets have remained calm.[45] It is worth considering, however, the uneven distribution of risks that asset confiscation might pose. To assess the vulnerability of G7 debt markets to foreign capital flight or retaliation, Figure 13 presents the

[45] See "Eurozone sovereign debt crisis? ECB warns of fiscal and growth risks," Euronews, and the ECB's financial stability review (published in November 2024) here.

spectrum of member countries' indebtedness and the foreign holdings of their debt. The most vulnerable countries are France and Belgium. They share three characteristics that make them vulnerable to destabilized sovereign debt markets. *First*, they each have relatively high debt to GDP ratios, particularly in comparison to other EU countries. *Second*, they have large shares of sovereign debt held by foreigners. *Third*, they are both politically vulnerable to retaliation. Belgium, as the home of Euroclear and therefore the jurisdiction of most of Russia's frozen assets, and France, the most vocal proponent of European independence, are both logical targets for foreign states unhappy with Russian asset confiscation. Non-EU members in the G7 are relatively insulated from retaliatory attacks on their debt markets. Japan, for example, despite its high debt to GDP rate, is protected by the fact that nearly all of its debt is held domestically. Canada, the UK, and the US are also helped by high shares of domestically-held debt that cushion their relatively high debt to GDP ratios.[46]

Figure 13: European debt to GDP ratios and share of debt held by foreigners (2023), in %

Source: Eurostat, KSE Institute

Counterargument: Policy Instruments Are at Our Disposal

The ECB has the instruments to deal with a politically motivated attack on European countries' debt. Some countries have already sent stern warnings that they would not be holding debt of countries that would seize Russian assets.[47] It is worth noting that the pressure is coming not from markets-related issues: fiscal irresponsibility of countries, legal unpredictability in the EU, risks to the Euro, or global financial contagion. It is coming from countries that are unhappy that the EU is taking a decision that Russia—which has violated the rules of international engagement (sovereignty of a country that is aspiring to join the EU) and threatens EU members[48] and their right to self-determination—should not enjoy the benefits of global international cooperation. The ECB has short-term and long-term instruments to fend off a politically motivated attack on an EU member government's market. First, the Transmission Protection Instrument (TPI) can be used.[49] Such an attack on one

[46] See "Sovereign debt investor base for advanced economies," updated in December 2024, from the IMF.
[47] Saudi Arabia is said to have warned the G7 that it would sell off European debt holdings if it seized Russia's assets. See "Saudis warned G-7 over Russia seizures with debt sale threat," Bloomberg.
[48] Putin has explicitly threatened Europe with retaliation for Ukraine's use of long-range missiles, ex-president Dmitry Medvedev frequently threatens European countries with nuclear strikes, and the Kremlin attempted to assassinate European defense industry executives.
[49] See "The Transmission Protection Instrument," ECB.

of the EU governments' bonds is exactly the time to use such an instrument. The instrument states that it "can be activated to counter unwarranted, disorderly market dynamics that pose a serious threat to the transmission of monetary policy across the Euro area." Second, should a longer-term solution be needed, however unlikely, the ECB can move on to use the Outright Monetary Transactions (OMTs) mechanism.[50] The instrument has some disadvantages as it was not designed for external shocks, but rather stability concerns related to a country's macroeconomic outlook and therefore requires that the respective country be in a European Financial Stability Facility/European Stability Mechanism (EFSF/ESM) program. On the plus side, there are no limits set on the size of the program. However, we believe that the threat of the ECB to use "whatever it takes" to protect financial stability in the Eurozone should be enough to prevent such an attack.

Concerns Related to Economic Precedent

Summary of Concerns

By confiscating the CBR's immobilized reserves, critics say that the West risks setting a geoeconomic precedent that may prove to be a future liability. *First*, it may threaten global faith in the sanctity of a state's reserve assets.[51] *Second*, and more importantly for the West, it may discourage foreign investment[52] and normalize corporate asset expropriation as an appropriate response to such an action. The latter scenario may be particularly threatening for the US, whose corporations hold enormous assets in China.

Counterargument(s): The status quo *already* sets a precedent

While critics of asset confiscation commonly raise the question of precedent, they often neglect the precedent that *inaction* sets. It is generally accepted that central bank reserves are sacrosanct, and that this is a worthwhile principle because it facilitates international commerce and respects state sovereignty. Thus, in a vacuum, confiscating reserves would risk undermining these key pillars of international cooperation. The choice is not, however, between undermining the sanctity of sovereign assets and doing nothing. Opting not to confiscate Russian assets sets its own precedent: namely, that a country can wantonly engage in a war of conquest and repatriate its reserves afterwards. Though ostensibly done in the name of the rules-based order, choosing not to confiscate CBR assets would show any would-be aggressors how its central tenet—state sovereignty—can be disregarded. It would pose the question why Russia's reserve assets abroad enjoy stronger protections than key tenets of international law, including the inviolability of a country's sovereignty and territorial integrity.

Russia's threat to seize Western corporate assets as retaliation poses less of a risk for economic precedent. First, Russia has already seized assets from Western corporations. An escalation of this practice hardly creates a new precedent. Second, while there is a legal basis for seizing Russian assets as a countermeasure, there would be no such basis for Russia's retaliation against Western companies.

[50] See "Technical features of Outright Monetary Transactions," ECB.
[51] See "Now is not the time to confiscate Russia's central bank reserves," Bruegel. The precedent could also allow countries not a party to wars to seize assets: see "The west would harm itself with rash seizures of frozen Russian assets," Financial Times; "Why using Russian assets to fund Ukraine is fraught," Bloomberg; "UK-France tensions over plan to seize $350bn Russia assets for US arms," The Guardian.
[52] See "UK-France tensions over plan to seize $350bn Russia assets for US arms," The Guardian.

Concerns Related to Retaliatory Actions by Russia

Summary of Concerns

Foreign companies with business interests in Russia as well as observers are concerned that Russia will significantly expand its campaign of asset expropriation if G7 countries make good on their threats to seize the CBR's immobilized reserves. Not only would this create meaningful costs for these businesses, they say,[53] but also provide Russia with a significant amount of money to pay for its war of aggression against Ukraine. Some commentators have pointed out that the value of the assets—those that remain in Russia and the regime might expropriate—is as large or larger than Russia's immobilized sovereign assets abroad.

Counterargument: Governments Should Not Socialize the Costs of Risky Business Decisions

It would be extremely problematic if governments refrained from confiscation of Russian assets abroad in order to protect the business interests of companies that made the deliberate decision to operate in Russia—and to continue to do so after the start of Russia's full-scale invasion of Ukraine. They would leave a bill of at least €230 billion for the support and reconstruction of Ukraine to their taxpayers while creating a dangerous moral hazard. Foreign companies operating in Russia have been perfectly aware of the heightened risk. Russia has already adopted measures amounting to expropriation against a number of foreign companies and enacted legislation severely restricting rights of Western investors. It has been implementing such steps from the early days of the full-scale invasion and, importantly, these steps represent the continuation of a long-standing practice of corruption and attacks on foreign companies' interests, which these businesses knew about and which they incorporated—or, at least, should have incorporated—into their risk assessments.

In addition, investors have a number of remedies available to them, including a well-established mechanism of international investment arbitration. While it is true that Russia has never voluntarily complied with any of the decisions of investment arbitration tribunals rendered against it, this is a consideration that should have entered companies' risk assessments with regard to their activities in Russia as well. But, legally speaking, the EU, in its 14th sanctions package, set up a new mechanism that enables EU companies to seek monetary compensation from Russian individuals or entities who benefited from asset expropriation. Aside from potential expropriation, the continuation of business in Russia may raise serious concerns regarding companies' complicity in the crime of aggression or their involvement in human rights violations. Therefore, such companies are in no position to demand that governments inform their foreign policy decisions by the need to protect their private commercial interests.

Companies should have been aware of the risks of doing business in Russia. Russia has long been known for a number of high-profile instances of stripping investors of their rights, with Yukos[54] and Hermitage Capital[55] among the most notable. The country's long history of rule-of-law deficits, which extends far beyond the last three years, was—or, at least, should have been—an important factor in companies' decisions to enter the Russian market and/or remain there. Russia ranks poorly in the Heritage Foundation's Index of Economic Freedom (43rd out of 44 countries in Europe). Prior to 2024, the country had consistently been ranked as "mostly unfree" in terms of economic freedom, reflecting challenges in areas like property rights and freedom from corruption.[56] In short, Russia's complete disregard for the rule of law and property rights is not a post-2022 development.

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[53] See "Confiscating sanctioned Russian state assets should be the last resort," Chatham House; "Russia can't match a Western asset seizure, but it can inflict pain," Reuters; "Why using Russian assets to fund Ukraine is fraught," Bloomberg; "A debate is centered on what to do with $300 billion in seized Russian assets," NPR; "Russia's frozen assets present a policy dilemma," Carnegie.
[54] See "Yukos Universal Limited (Isle of Man) v. The Russian Federation," PCA Arbitration.
[55] See "William Browder, Hermitage Capital, the Russian State and the Case of Sergei Magnitsky," Chatham House.
[56] See "Economic freedom country profile: Russia," Heritage.

During the full-scale invasion, the US Department of State issued a business advisory warning investors about heightened risks associated with Russia.[57] Specifically, it noted that: "doing business in the Russian Federation and in Russia-occupied territories of Ukraine poses serious legal, financial, and reputational risks. Russia's kleptocratic environment undermines fair competition and the rule of law, making businesses susceptible to extortion, property seizures, and US law enforcement action." Further, the US government articulated the following risks posed by working in Russia: "1. Risk of businesses and individuals becoming exposed to sanctions, export controls, import prohibitions, money laundering vulnerabilities, and corruption; 2. Risk of businesses and individuals being implicated in the Government of Russia's violations of international law, including war crimes and crimes against humanity, and human rights abuses; and 3. Risk to businesses and individuals due to the proliferation and implementation of repressive laws in the Russian Federation and the areas of Ukraine it occupies, including measures authorizing expropriation in certain instances or detentions based on spurious grounds."

Russia's discriminatory and repressive measures are the continuation of a long-standing practice. According to KSE Institute,[58] starting from early 2022, foreign investors have incurred over $167 billion in direct losses caused by the need to urgently withdraw from Russia. These losses include assets write-offs, the impact of illegitimate court rulings, and business expropriations. Total write-offs for 301 companies, whose assets were expropriated, exceed $57 billion, with the assets' original value estimated at ~$74 billion. Additionally, "exit taxes"[59] imposed by Russia have placed further financial strain on foreign businesses, amounting to at least 250 billion rubles (~$2.7 billion) between 2023 and mid-2024. These losses were not incurred because the West froze CBR assets; they were incurred because Russia does not respect property rights.

Starting from March 2022, the Russian government moved to adopt legislative amendments aimed at limiting capital outflows and precluding Western businesses from exiting Russia. Importantly, restrictive measures exclusively affect investors affiliated with so-called "unfriendly" states. The list contains more than 50 states and territories, including the United States, all EU member states, Ukraine, the United Kingdom (including all British Overseas Territories and Crown Dependencies), Australia, Canada, Norway, and Switzerland.[60] First, between March and October 2022 Russia introduced several regulations, whereby individuals and entities associated with "unfriendly" states cannot transfer funds outside Russia. The ban concerns not just repatriation of investments but also the paying out of FX loans.[61] Second, since January 2023, Russian companies with foreign investors can legally disregard votes cast by foreign investors (affiliated with "unfriendly" states) or their representatives

[57] See "Risks and Considerations for Doing Business in the Russian Federation and Russia-Occupied Territories of Ukraine," US Department of State.

[58] See "Assessing foreign companies' direct losses in Russia: financial impact, market consequences, and strategic adjustments", KSE Institute.

[59] See an extract [ru] from the minutes of the meeting of the subcommittee of the Government Commission for control of foreign investments in the Russian Federation dated October 15, 2024 N 268/1, which stipulates an obligation to make "voluntary" contributions to the federal budget of at least 35% of the market value of the assets. As we understand from the current legislation, the "market value" is understood to be the one stated by the approved appraisal provider.

[60] See Russia's Governmental Decree No.430 of March 5, 2022 approving a list of "unfriendly" states.

[61] On March 1, 2022 the Russian Central Bank circulated a letter [ru] establishing a ban on all bank transfers abroad from bank accounts of individuals and legal entities from "unfriendly" states. On March 5, 2022, Presidential Decree No.95 [ru] "On the Temporary Procedure for Complying with Obligations owned to Certain Foreign Creditors" was issued, establishing special procedure for repayment of loans and performance under other financial instruments issued by creditors from "unfriendly" states. Payments under such obligations exceeding 10 million rubles per month can only be made in rubles (regardless of the contractual terms), and to a special type "C" account in Russian banks exclusively. On March 5, 2022 Ministry of Finance issued a clarification [ru], stating that restrictions imposed by Decree No.95 also apply to payment of dividends to foreign shareholders (affiliated with "unfriendly" states) of Russian joint-stock companies. An October 15, 2022 Presidential Decree No. 737 [ru] "On Certain Aspects of Performing Certain Types of Transactions" - imposes restrictions on funds distributions to entities affiliated with "unfriendly" states in relation to the liquidation of Russian-incorporated companies, the reduction of the charter capital of such companies, and in course of procedures related to bankruptcy.

on boards of directors or supervisory boards.[62] Third, since September 2023, Russian law allows the "suspension" of corporate rights of shareholders affiliated with "unfriendly" states. Suspension under this law effectively means the expropriation of all shareholder rights.[63]

Tellingly, some of the most repressive measures were introduced by Russia immediately after particularly strong statements of Western governments *ruling out* asset seizure. On May 18, 2022, it was reported that US Treasury Secretary Janet Yellen stated the following about the confiscation of Russian assets: "While we are beginning to look at this, it would not be legal now in the United States for the government to seize those [assets]… It is not something that is legally permissible in the United States."[64] On May 24, 2022, a draft Federal Law "On External Administration for the Management of an Organization,"[65] allowing for taking over the companies that attempt to exit Russia, was approved by the Russian Parliament in the first reading. On 18 April 2023, it was reported that European authorities found that they had no legal means for confiscating Russian assets, and that such assets must be returned to Russia after the war.[66] On April 25, 2023, Russia issued Presidential Decree No. 302 "On Temporary Management of Certain Assets, Including Movable and Immovable Assets And Equity Interests In The Capital Of Russian Legal Entities."[67] The decree established a legal basis for expropriation of foreign companies through the procedure of enforced appointment of outside managers, similar to bankruptcy procedures. It stipulates a rather broad and open-ended definition of the events that may trigger the such a step: (i) deprivation of the Russian Federation, Russian legal entities or individuals of the right to property located in the foreign state; (ii) restrictions of their property rights, the event of threat of such deprivation or restrictions of property rights, the event of threats to national, economic, energy, or other types of security of the Russian Federation.

Based on this decree the following companies were expropriated: JSC Fortum (owned by Finland's majority state-owned Fortum Oyj); Unipro, owned by German state-owned Uniper SE; Danone Russia JSC (owned by French investors); Company Baltika LLC[68] (owned by Carlsberg), Bosch, and others. Oftentimes, companies put under "temporary management" are sold on concessionary terms to entities associated with Russian elites. For instance, Deputy Chairman of the Chechen government and nephew of Chechen strongman Ramzan Kadyrov was appointed as CEO of Russian Danone Business in July 2023,[69] and in December 2024 the company was acquired by the former deputy minister of agriculture of the Chechen Republic.[70] Presidential Decree No. 302 remains the primary mechanism through which the Russian government appropriates Western assets.

Continuation of activities creates the risk of corporate complicity in international crimes. Expropriation of assets is not the only risk that companies had to assess when making decisions about remaining engaged in Russia. There are grounds to consider whether businesses continuing working in Russia can be economically complicit in the crime of aggression, or even implicated in the commission of war crimes or gross violations of human rights. This raises further questions regarding the efforts that should be undertaken to protect these entities from the consequences of their business decisions. First, as previously proposed by KSE Institute,

[62] See the Kremlin's Presidential Decree No. 16 [ru]"On the Temporary Procedure for Decision-Making by the Governing Bodies of Certain Russian Business Enterprises" of January 17, 2023.
[63] See Russia's Federal Law No. 470-ФЗ [ru] "On Certain Aspects of Regulating Corporate Relations in Business Entities that are Economically Significant Organizations" from September 4, 2023.
[64] See "Yellen: Not legal for U.S. to seize Russian official assets," Reuters.
[65] See draft Federal Law N 104796-8 [ru] "On External Administration for the Management of an Organization."
[66] See "EU concludes authorities cannot seize Russian assets," Central Banking.
[67] See the Kremlin's Presidential Decree No. 302 [ru]
[68] In December 2024 the restrictive measures towards Baltika LLC were lifted [ru].
[69] See "The new head of "Danone Russia" is the Deputy Chairman of the Chechen government and Kadyrov's nephew," Forbes Russia [ru].
[70] See "The former Deputy Head of the Chechen Ministry of Agriculture has become the owner of Danone's former assets in Russia," Forbes Russia [ru].

Russia appears to be pursuing strategy of civil-military fusion,[71] and Russian law mandates that private companies can be obligated to take on state military procurement contracts if the Russian government decides so. Specifically, In July 2022, the Russian parliament enacted federal law No. 272-ФЗ ("On Amending Certain Legislative Acts of Russian Federation"), whereby businesses in Russia cannot refuse entering governmental procurement contracts in general, and military procurement contracts in particular, if they are deemed necessary by the government to ensure the conduct of foreign counter terrorism and other operations by the Russian armed forces. Further, a US Government Business Advisory highlights this risk by stating that "businesses are being forced to cooperate in Russia's military mobilization and could be implicated in Russia's commission of war crimes and crimes against humanity as part of Russia's brutal war against Ukraine."[72]

The law of corporate criminal complicity in international crimes is still in the state of development, with certain notable cases that can establish precedent for prosecution of multinationals operating in Russia during the full-scale invasion of Ukraine. One of the examples are the pending criminal proceedings against international banking group BNP Paribas following the bank's activities during the civil war in Sudan. Initially, BNP Paribas, S.A. and its subsidiary in Geneva faced multiple legal proceedings related to violation of financial sanctions when operating in Sudan during armed conflict. In 2015, the Bank pleaded guilty in US Federal Court in the Southern District of New York to violating US sanctions in Sudan, Iran, and Cuba. Subsequently, BNP Paribas paid a $8.9 billion penalty to the US government.[73] The facts disclosed in the plea agreement[74] provided enough grounds for human rights advocates to initiate a number of civil and criminal cases against the banking group worldwide. The bank is also currently the subject of a judicial criminal investigation in Paris for alleged financial crimes (money laundering and concealment) and complicity in international crimes, namely torture, crimes against humanity, and genocide, committed in Sudan between at least 2002 and 2008.[75] The judicial investigation, opened in 2020, was triggered in response to a criminal complaint filed in 2019 by Sudanese victims of these crimes (and two French non-governmental organizations). The investigation remains active. The judges may charge the bank and its subsidiaries as well as any individuals that may be considered responsible. Because of the complexity of the investigation, it is expected to take several years to complete. Another pending case regarding a major international corporation's complicity in human rights violations committed by a foreign government is Doe VS. Cisco System, which is currently being considered by US courts. This case does not involve violation of sanctions—alleged complicity in human rights violations arises from ostensibly fully legitimate business operations.[76] Finally, legal scholars have begun discussing the concept of economic complicity in the crime of aggression by virtue of paying taxes in the aggressor state, knowing that the lion's share of tax revenues are used to finance the war effort.[77]

Investors' rights are—theoretically—protected through investment treaty arbitration. Investment treaty arbitration is a rational choice for protecting investors' rights in case of asset expropriation or other violations. Russia is a party to over 60 bilateral investment treaties ("BITs") with most EU members (such as Austria, Belgium, Bulgaria, the Czech Republic, Cyprus, Denmark, Finland, France, Germany, Greece, Hungary, Lithuania, Italy, Luxembourg, the Netherlands, Norway, Romania, Slovakia, Spain, and Sweden), and other

[71] See "Challenges of Export Control Enforcement," KSE Institute.
[72] See "Risks and Considerations for Doing Business in the Russian Federation and Russia-Occupied Territories of Ukraine," US Department of State.
[73] See "BNP Paribas Sentenced for Conspiring to Violate the International Emergency Economic Powers Act and the Trading with the Enemy Act," US Department of Justice; "BNP Paribas Agrees to Plead Guilty and to Pay $8.9 Billion for Illegally Processing Financial Transactions for Countries Subject to U.S. Economic Sanctions," US Department of Justice.
[74] See "United States of America v BNP Paribas, S.A.," para 17, United States District Court Southern District of New York.
[75] See "Sudanese victims ask French judges to investigate BNP Paribas' role in atrocities," International Federation for Human Rights.
[76] The case is discussed in some details in "Challenges of Export Control Enforcement," KSE Institute.
[77] For further details, please see "War Funders and Profiteers: Economic Complicity in International Crimes in Ukraine and Beyond," Moiseienko et al.

countries such as Canada, Japan, Korea, Switzerland, the UK.[78] There is no BIT between Russia and the United States, but US companies may nonetheless initiate investment arbitration if they structured their investments in Russia through a jurisdiction that does have a Russian BIT.

It appears that Russia's restrictive measures discussed above violate nearly all internationally accepted standards of investment protection incorporated in most BITs, such as: fair and equitable treatment of investors, protection from unlawful expropriation (direct and gradual), freedom of transfer of capital, national treatment standards, and most-favored-nation standards. Most BITs and multilateral investment agreements, such as the Energy Charter Treaty, contain clauses requiring states to provide "fair and equitable treatment" ("FET") to investors and/or investments from the other contracting party/parties. FET standards include protection from discrimination, transparency requirements, and respect for investors' legitimate and reasonable expectations.

Many of the legislative amendments adopted in Russia since its full-scale invasion of Ukraine lead to a direct or "creeping" expropriation of foreign investments. The international investment protection regime prohibits expropriation of investments except when it is done with prompt and adequate compensation, for a public purpose, in accordance with due process, and on a non-discriminatory basis. According to arbitral practice, such prohibitions include not only direct expropriation, but also a broad spectrum of measures, often termed "creeping expropriation."[79] Although precise data remains limited, KSE Institute has documented at least 30 cases of foreign companies whose assets were expropriated by the Russian government since 2022.[80]

The most obvious regulation to consider in the context of unlawful expropriation is the aforementioned Presidential Decree No. 302 of 25 April 2023, which mandates the appointment of the Federal Agency for State Property Management as the temporary manager of certain companies and/or assets. According to the decree, the imposition of a temporary manager can be triggered by a broadly and vaguely drafted set of circumstances. Further, the Federal Property Agency can exercise all rights of the owner of such assets, except for their disposal. Outside management is ostensibly a temporary measure, however, it can be terminated only by a decision of the president of the Russian Federation. Most companies affected by Decree No. 302 announced their plans to exit Russia back in 2021-2022, sometimes even before the full-scale invasion and the imposition of Western sanctions. In March 2022, Fortum announced[81] a suspension of all new investment projects and financing in Russia, and, in May 2022, the company announced that it was seeking a controlled exit from the Russian market. Uniper notified the Russian government of its intention to sell its Unipro stake in 2021. Similarly, Carlsberg[82] and Danone[83] both announced their plans to exit Russia and halted new Russian investments in 2022. Based on publicly available information, only one of the affected companies, Fortum,[84] formally sent notices of arbitration to the Russian Federation at this point.[85] As demonstrated by the Unipro case, the targeting of certain companies is often triggered by their attempt to exit the Russian market. Additionally, Vice Prime Minister and Minister for Trade and Industry Denis Manturov stated[86] that Russia shall "actively invoke temporary management at the

[78] See a list of international investment treaties binding Russia at UNCTAD's Investment Policy Hub.
[79] As articulated by UNCTAD: "[c]ertain governmental measures may not involve an actual physical taking of property, but may still result in the effective loss of management, use or control, or a significant depreciation of the value, of the assets of a foreign investor."
[80] See "Assessing foreign companies' direct losses in Russia: financial impact, market consequences, and strategic adjustments", KSE Institute.
[81] See "Fortum's exit from the Russian market," Fortum.
[82] See Interfax [ru].
[83] See "Danone announces it plans to transfer the effective control of its EDP business in Russia," Danone.
[84] See "Fortum has sent notices of dispute to the Russian Federation due to the violations of international investment treaty protection," Fortum.
[85] See a list of pending investment treaty arbitrations with Russia as a respondent state at UNCTAD's Investment Policy Hub.
[86] See here [ru].

entities owned by "bad faith investors." He explained that the term "bad faith investors" denotes companies who remained in Russia but suspended further investment projects.

Even though Decree No. 302 and Russian official commentators allege that the original owners of the assets retain the legal title to such assets, it is rather obvious that, in fact, foreign shareholders lost any control over them. The imposition of temporary external administration was specifically recognized to be a measure amounting to expropriation by international tribunals. In Payne v. Iran, the outside managers were appointed on a "provisional" basis but the respective Iranian law "did not prescribe the length of government control and did not provide for judicial or administrative determination of whether the property should be returned to its original owners."[87] The tribunal concluded: "[w]hile one of the purposes of the Law of 16 June 1979 is the appointment of managers on a "provisional" basis, the sum effect in this case was the deprivation of any interest of the original owners in the companies once they were made subject to provisional management by the Government." It is also important that the tribunal determined the date of imposition of "provisional" managers as the date when effective expropriation took place: "if at "the date of the government appointment of "temporary" managers there is no reasonable prospect of return of control, a taking should conclusively be found to have occurred as of that date."[88]

In the case of Russia, investment arbitration is unlikely to yield results for foreign companies. Russia has never voluntarily complied with any of the decisions of investment arbitration tribunals rendered against it.[89] Currently, Ukrainian companies that prevailed in Crimean-related arbitrations actively work on enforcing awards against Russia abroad, and Yukos shareholders have been trying to enforce the record $50 billion award for over a decade.[90] Interestingly, in 2015, Russia sent a diplomatic note to the French government threatening to retaliate against French companies and individuals should France move to freeze Russian assets based on the Yukos arbitration award. Reportedly the note stated: "Any attempt to undertake injunctive measures or measures of execution against Russian property located on the territory of the Republic of France will be seen by the Russian Federation as grounds to take adequate and proportional retaliatory steps against the Republic of France, its citizens, and its legal entities."[91] Threatening the expropriation of someone else's assets is clearly a standard operating procedure of the Russian regime. It should be noted that freezing foreign assets as a part of enforcement procedures arising out of investment arbitration is not an extraordinary event; legal grounds and procedures for such actions are usually set in most civilized jurisdictions. There is no uncertainty as to whether France was acting within the bounds of international as well as national law; nevertheless, Russia chose to threaten to retaliate against the state, as well as private companies and individuals. France was not deterred by Russia's baseless claims and did freeze the property relevant to enforcement proceedings.[92]

Further, the Russian legal system expressly stipulates the priority of Russian law over international law, and subjects decisions of international courts and tribunals to judicial review by Russian courts. In 2015, Russia enacted a law authorizing the Constitutional Court to decide whether to comply with decisions of international human rights courts. In 2020, Russia enacted constitutional amendments that, among other things, allow Russia to disregard decisions of any international courts and tribunals.[93] Specifically, Article 79 of the Russian constitution reads: "Decisions of interstate bodies adopted on the basis of the provisions of international treaties

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87 See Thomas Earl Payne v. The Government of the Islamic Republic of Iran, IUSCT Case No. 335 here.
88 See Payne v. Iran, para. 20, 23.
89 See "State Compliance with Investment Awards," Emmanuel Gaillard and Ilija Mitrev Penusliski.
90 See "Russia continues pressing sovereignty claims in the Yukos award saga," Transnational Litigation Blog.
91 See "Russia warned France of reprisals months before Yukos asset freeze," Radio Free Europe.
92 French authorities have seized dozens of bank accounts and several buildings owned by the Kremlin. See "France freezed Russian assets," DW.
93 See Russia's federal law "On Amending Federal Law on the Constitutional Court of the Russian Federation" of December 14, 2015, here [ru].

of the Russian Federation which in their interpretation contradict the Constitution of the Russian Federation, shall not be implemented in the Russian Federation."

The adverse factors described above are a part of public record and have been known to the businesses, which initially decided to invest in Russia and continued working in the country after 2022. Finally, it is important to remember that, when businesses demand that their governments should move to protect them from Russia's oppressive measures or to act in a manner not to provoke further deterioration of the legal regime in Russia, their home states have already played their role by entering into a BIT. The system of investment treaties was established to replace the diplomatic protection mechanism previously used by states to protect interests of their nationals and companies in foreign states, whereby the state would bring a public international law claim or exercise other measures on behalf of its nationals.[94] Through the BIT mechanism, the state-parties expose themselves to claims from private actors in exchange for gaining the same privilege for their nationals.

EU companies suffering from expropriatory measures are protected through a new legal mechanism. On June 24, 2024, the EU adopted Council Regulation 2024/1745,[95] which imposes the 14th package of sanctions against Russia. Article 11b(1) establishes a legal mechanism enabling EU companies to seek monetary compensation from Russian individuals or entities who have benefited from asset appropriation measures implemented through Russia's repressive legislation, such as Decree No. 302 (discussed above). Specifically, the regulation allows bringing claims against Russian listed entities, entities outside the Union whose proprietary rights are directly or indirectly more than 50% owned by listed entities, as well as any Russian natural or legal person and any person acting through or on behalf of them. The regulation further mandates that claimants can resort to this mechanism as a result of lack of effective access to remedies under the relevant jurisdiction, which should include inability to protect their right in the Russian judiciary or through international investment arbitration. Thus, the EU has already undertaken significant steps to protect the interests of its companies.

Counterargument: Expropriation of Company Assets Is Not a Legal Response to Asset Confiscation

Russia wants to draw a connection between the expropriation of foreign companies' assets and the potential confiscation of Russian sovereign reserves abroad. These measures are fundamentally different, however. As has been outlined by many legal experts, the confiscation of Russian sovereign assets is legal as a third-party countermeasure on behalf of Ukraine, undertaken by its allies, and conducted in response to Russia's gross and persistent violations of key tenets of international law, including the prohibition of wars of aggression and the principles of inviolability of sovereignty and territorial integrity.[96] Russia's actions, on the other hand, are illegal. International law does not justify countermeasures in response to countermeasures. The Russian state violated international law—these companies did not. Equating the confiscation of CBR reserves and Russia's expropriation of foreign companies muddies the legal waters and accepts a false Russian narrative.

Counterargument: Large-Scale Expropriation of Foreign Companies' Assets Is Not in Russia's Interest

Regardless of when Russia's war in Ukraine ends, it is clear that Moscow is keen to bring Western business and investment back to its economy. The Kremlin—and, at times, seemingly the White House—is hoping for economic normalization between Russia and the West, with or without peace in Ukraine.[97] If Russia

[94] The last notable diplomatic protection investment dispute was Barcelona Traction, Light and Power Company, Limited brought by Belgium against Spain to the International Court of Justice, available here.
[95] Available here.
[96] See "Legal report on confiscation of Russian state assets for the reconstruction of Ukraine," KSE Institute.
[97] See "Trump's Moscow mirage: profits for a select few," Carnegie; "Putin ally pushes deal to restart Nord Stream 2 with US backing," Financial Times; "Russia, US discussing rare earth metals projects, Putin envoy says," Reuters.

decides to nationalize Western private sector investments within its borders en masse in retaliation for losing its CBR assets, it will effectively deter future Western investors.[98] From the standpoint of a Western multinational or investor, it is hardly relevant *why* Russia seized corporate assets—it is relevant only that it *did*, and that it could again. It could take decades for Russia to regain the trust of international markets, which is likely an unacceptable risk for the Kremlin. Thus, the threats of widespread seizure of Western corporate assets ring hollow.

Counterargument: Foreign Assets Are Likely Illiquid to a Significant Extent

Little is known about the total value of foreign individuals' and companies' assets in Russia, which may become the target of expropriatory actions by the Russian regime. While a full accounting of foreign investments from "unfriendly" countries is impossible due to serious data restrictions, we can approach the question from two angles: (1) a bottom-up accounting of individual companies' assets resulting in a lower bound estimate or (2) a top-down analysis of official investment data resulting in an upper bound estimate (see Table 1).

Table 1: Estimates of foreign assets remaining in Russia

Source	Type of investment	Estimated amount	Liquid/illiquid
Leave-Russia	Total assets held by companies from G7 countries	$131 billion	Mixed
IMF	Portfolio investment	$43 billion	Liquid
CBR	Foreign holdings of Russian sovereign debt (OFZ)	~$11 billion	Liquid
CBR	Amortized holdings of OFZs, now likely in cash	~$25 billion	Liquid
IMF	FDI	$108 billion	Illiquid

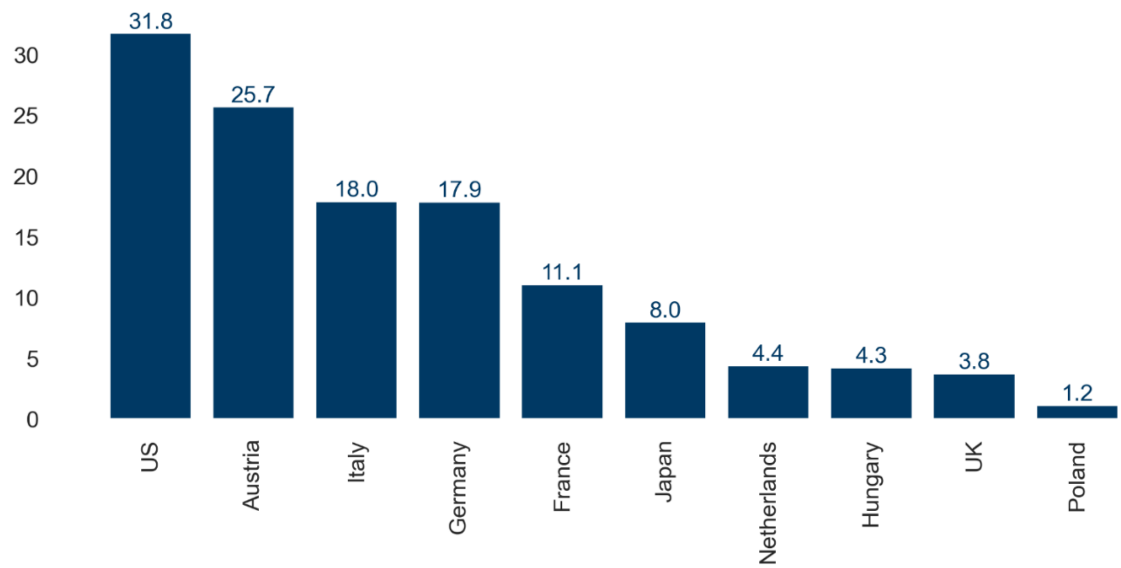
First, we can calculate the reported assets and losses of foreign companies. KSE Institute's Leave-Russia project, which has tracked the status of foreign companies operating in Russia since 2022, estimates that the total assets of foreign companies still operating in Russia stood at $190 billion at the end of 2023.[99] Of these assets, $131 billion belonged to entities from G7 countries, with companies from the United States, Austria, Italy, Germany, and France accounting for the largest amounts (see Figure 14). Compared to the losses (from write-offs and seizures) reported by foreign companies—over $160 billion accounted for by entities from the G7—over half of the potential impact has already materialized.[100]

Second, we can supplement IMF data on the positions of foreign investors with statistics from the CBR to estimate the value of investments in Russia before and after its full-scale invasion. This approach is less precise but provides a solid upper bound for our calculations. Investments are divided into portfolio investments (passive investments like holdings of stocks and bonds) and foreign direct investment, or FDI (longer term, active investments). IMF data shows that $43 billion in foreign portfolio investment were held by actors in G7 countries at the end of 2023.[101] At the time of Russia's full-scale invasion of Ukraine, foreign investors were also heavily involved in the market for domestically-issued Russian sovereign debt, so-called OFZs (Облигации федерального займа), holding almost three trillion rubles in such securities.[102] As of early-2025, holdings have fallen by more than two trillion rubles and, as the trade with these assets is sanctioned in many jurisdictions, this likely means that the bonds matured and turned into cash. Due to Russian restrictions on cross-border transactions, especially by entities from "unfriendly"

[98] See "Emboldened Kremlin steps up efforts to seize businesses in Russia," New York Times.
[99] Leave-Russia's public database can be accessed here.
[100] See "Assessing foreign companies' direct losses in Russia: Financial impact, market consequences, and strategic adjustments," KSE Institute.
[101] Includes the member countries of the G7 as well as member states of the European Union. See "Portfolio investment positions by counterpart economy (formerly CPIS)," IMF. It is worth noting that this data does not appear to capture all non-resident holdings in Russia, which the CBR measured at $148 billion at the time, and, thus, may underestimate the amount of assets at risk
[102] See "Russia Chartbook" February 2025 edition, KSE Institute.

states, this money—close to $25 billion at an exchange rate of 85 rubles per dollar—likely remains in Russia and could become the target of expropriation. Aside from these amortized securities, non-residents—to a large extent from "unfriendly" countries—continue to hold around $11 billion in OFZs. Portfolio investments and cash in Russian bank accounts should be considered likely targets for expropriation as these assets can be used quite easily.

Figure 14: Assets of foreign companies in Russia, in $ billion



Source: KSE Institute

FDI is a larger—and more ambiguous—stockpile of assets held in Russia. According to the Russian central bank, a large share of foreign investment positions is in the form of FDI (43% of the total at the end of 2024) and other investment (37%), with portfolio investment only accounting for 20%.[103] While this data captures *all* foreign investors and not just those from "unfriendly" countries, it shows that the problem likely extends significantly beyond portfolio holdings. Unfortunately, the IMF's data in this regard shows only *net* inward positions (i.e., liabilities minus assets). Furthermore, it also identifies large FDI holdings in countries such as Cyprus, which have been traditionally used by Russians for purposes of tax evasion and the set-up of opaque investment mechanisms—and where confiscation is therefore not likely. Taking the IMF data at face value, holdings of G7 countries (excluding Cyprus) amounted to $108 billion at the end of 2023.[104] This is 35% of all foreign direct investment in Russia captured by the IMF's data ($303 billion). Until the start of the full-scale invasion, Russia's central bank also published a detailed accounting of FDI positions by country. At the end of 2021, it showed G7 holdings of $245 billion (or 40% of the total)—again, excluding Cyprus as well as tax havens in overseas territories, where a similar argument regarding the risk of confiscation applies. Importantly, direct investment is by definition less flexibly usable in case of expropriation. In other words, a foreign owned factory would have to be sold to an investor in Russia to generate money that can be used by the regime.

One additional issue deserves consideration: so-called Type "C" accounts. Starting from March 2022, Russian law has allowed entities incorporated in Russia and affiliated with "unfriendly" states to receive payments exclusively

[103] See "External sector statistics," CBR.
[104] See "Direct investment positions by counterpart economy (formerly CDIS)," IMF.

in special Type "C" bank accounts and in rubles—regardless of the original contractual terms.[105] The regulatory framework essentially freezes these funds as transfers are only allowed in a very limited number of circumstances, including, primarily, payments of taxes in Russia, purchases of Russian government bonds, certain payments to Russian entities, and bank commissions.[106] Importantly, no transfers outside of Russia are allowed. Restrictive measures are imposed on securities Type "C" repo accounts in a similar way. There is no reliable and transparent information regarding the amount of funds frozen on these accounts. The Russian government clearly attempts to make these funds seem comparable to the CBR's reserves immobilized in the West. For instance, while omitting the exact amount, Deputy Minister of Finance Alexey Moiseev stated in 2023: "We have a volume of frozen assets in 'C' type accounts that is comparable to the volume of frozen Russian assets located outside the Russian Federation."[107] However, publicly reported figures are considerably smaller. First, it was reported that there are 280 billion rubles (~$3.3 billion) accumulated on these types of accounts.[108] In March 2023, the CBR used the sum of 0.5 trillion rubles (~$5.9 billion) in its reporting.[109] Some Russian analysts speculated at the end 2022 that the total amount could reach 1 trillion rubles in 2023.[110] It is not entirely clear whether these sources referred to Type "C" cash accounts only or include repo Type "C" securities accounts in their estimates.

While more research on this issue is clearly needed, we believe that it is fair to conclude that a substantial share of the investments at risk of expropriation is not liquid, i.e., consists of production facilities and other fixed assets. Thus, their value does not immediately become available to the Russian state to wage war, alleviating the concern that confiscating CBR assets would lead to a tit-for-tat outcome where neither side is net better off.

Concerns Related to Leverage in Peace Negotiations

Summary of Concerns

Citing the fear that the Trump administration will force Kyiv and Moscow to the negotiating table in an unfavorable position for Ukraine, some observers consider the CBR reserves to be a valuable bargaining chip for Kyiv and its Western partners that should not be used prematurely. According to this logic, Kyiv would enter negotiations in a weaker position if the CBR reserves have already been seized.[111] On a related

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[105] Russian regulations capture all payments exceeding 10 million rubles per month, including repayment of loans and dividends, return of capital in case of company winding up or bankruptcy, payments in result of sale of shares, etc. For further details, see Presidential Decree No.95 [ru] of March 5, 2022 "On the Temporary Procedure for Complying with Obligations owned to Certain Foreign Creditors and Presidential Decree No. 254 [ru] of May 4, 2022 "On the Temporary Procedure for Performing Financial Obligations Pertaining to Corporate Relations Towards Certain Foreign Creditors", Presidential Decree No. 737 [ru] of October 15, 2022 "On Certain Aspects of Performing Certain Types of Transactions", Amendments [ru] to the rules on approving transaction on divesting from Russia, adopted by the Governmental Commission for Foreign Investment Control on 07 July 2023.

[106] The full list of transactions is stipulated in the Decision of the Board of Directors of Bank of Russia [ru] of June 24, 2022 and includes the following transactions: payment of taxes, duties, fees and other obligatory payments payable in accordance with the budget legislation of the Russian Federation; transfers for the purchase of federal bonds issued by the Russian Ministry of Finance; transfers to bank accounts of type "C"; transfers to brokerage accounts of type "C" and special brokerage accounts of type "C", trading bank accounts of type "C", clearing bank accounts of type "C"; payment of commissions to an authorized bank servicing the account; transfers to Russian residents in connection with the transfer of securities; transfers to Russian residents for payment of a penalties (fines, penalty fees) under certain transaction; return of funds erroneously credited to a type "C" bank account.

[107] See TASS [ru].

[108] See here [ru].

[109] See CBR [ru].

[110] See here [ru].

[111] See "Confiscating sanctioned Russian state assets should be the last resort," Chatham House; "The unintended consequences of seizing Russian assets," Foreign Policy; "Now is not the time to confiscate Russia's central bank reserves," Bruegel; "Seizing Russian assets: a feel good bill that will absolutely boomerang," Responsible Statecraft.

note, some fear that seizing the CBR reserves would fuel resentment against Western states, furthering the notion that the West does not abide by its own rules-based order. While this may not directly affect peace negotiations, it could undermine the West's ability to claim the moral high ground.[112]

Counterargument: Leverage in Negotiations Remains Independent of Confiscation

Countermeasures are based on the *Articles on State Responsibility for Internationally Wrongful Acts*, and Article 49(3) of the Articles states that countermeasures have to be reversible to the extent possible. It reads: "Countermeasures shall, as far as possible, be taken in such a way as to permit the resumption of performance of the obligations in question."[113] Even though this reversibility requirement is not absolute, reversible measures are preferred as they reflect the nature of countermeasures as an instrument to induce compliance, rather than serve a punishment. There is an understanding in international law that financial damage is generally reversible in nature, which would also apply to asset confiscation.[114]

In the case of the Russian reserves, reversibility must be discussed in the context of Ukraine's right to compensation from Russia for its illegal invasion and the damages caused. Ukraine's right is not disputed and was additionally confirmed by UN General Assembly Resolution ES-11/5, which stipulates that "the Russian Federation must he held to account for any violations of international law in or against Ukraine, including its aggression in violation of the Charter of the United Nations (…) and that it must bear the legal consequences of all its internationally wrongful acts, including making reparation for the injury, including any damage, caused by such acts."[115] Legal scholars argue that the requirement of reversibility would be satisfied if confiscated Russian sovereign assets are transferred to Ukraine, possibly to the future fund of the International Compensation Mechanism,[116] under condition that they are transferred back if and when Russia complies with its obligation of reparation.[117] "Russia would be credited with any reparations actually paid by the mechanism, and its remaining obligation (if any) would be correspondingly reduced. In the event the value of its transferred assets were to exceed the amount of reparations owed, the excess could be transferred back to Russia."[118]

If, indeed, the confiscation of Russia's sovereign assets abroad is reversible—by reducing the amount of future reparations—then the bargaining chip entirely remains on the table during negotiations. Instead of threatening confiscation in the event of certain violations of agreements, countries would threaten not to reverse the confiscation until certain conditions are fulfilled.

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112 See "The unintended consequences of seizing Russian assets," Foreign Policy; "Now is not the time to confiscate Russia's central bank reserves," Bruegel.
113 See "Articles on Responsibility of States for Internationally Wrongful Acts," UN International Law Commission.
114 James Crawford, "Counter-Measures as Interim Measures," European Journal of International Law, Vol. 5, Oxford University Press, 1994, pp. 65-76, p. 68, quoted by Phillipa Webb in "Legal options for confiscation of Russian state assets to support the reconstruction of Ukraine," European Parliamentary Research Service.
115 Available here.
116 See "Resolution CM/Res(2023)3 establishing the Enlarged Partial Agreement on the Register of Damage Caused by the Aggression of the Russian Federation against Ukraine," Council of Europe.
117 See "Legal options for confiscation of Russian state assets to support the reconstruction of Ukraine," Philippa Webb in the European Parliamentary Research Service.
118 See "On proposed countermeasures against Russia to compensate injured states for losses caused by Russia's war of aggression against Ukraine," IISS.