Impact of Expanded Sanctions Against Russia and Belarus on Financial Service Provision in the Baltics: A Business Perspective

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Specialized expertise report

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Executive summary

This preliminary investigative study examines the impact of the European Union's (EU's) expanded sanctions against Russia and Belarus — imposed following Russia's full—scale invasion of Ukraine in February 2022 — on the financial services available to businesses in Estonia, Latvia, and Lithuania. Given their historical and geographical proximity to Russia, Baltic states are particularly affected.

Using an exploratory survey and a focus group with selected businesses, the study examines whether businesses perceive disruptions in financial services due to sanctions, how these impacts affect both businesses and financial service providers, and it also explores potential ways to alleviate these challenges. The survey also highlights efforts by businesses and financial institutions to stay updated on evolving sanctions.

Gathering data on the impact of sanctions on businesses in the Baltic states proved challenging, as businesses were often reluctant to discuss potential negative effects for fear of reputational or regulatory repercussions. This reluctance was highlighted by the exploratory survey, which additionally identified key challenges businesses face. To gain deeper insights, a focus group was conducted with participants from eleven Baltic companies, including CEOs, compliance professionals, and financial service providers, under strict anonymity and the Chatham House rule. This approach successfully facilitated candid discussions, overcoming the initial "wall of silence." However, limitations remain, including potential reinforcement bias, as businesses most affected may be more willing to participate, and the small sample size is not fully representative of all types of businesses in the Baltic states. Despite these constraints, publishing these collective insights is essential to better understand the challenges businesses face and explore potential solutions.

Key findings:

- **Broad support for the expanded sanctions:** Research participants generally endorsed the sanctions and demonstrated active compliance efforts.
- **Negative business impact**: 85% of respondents reported moderate to significant disruptions to their business, with non-financial businesses more affected.
- **Financial service challenges**: 71% experienced delays and increased costs due to enhanced compliance, leading some businesses to seek financial services outside the Baltics, where sanction implementation is considered less strict.
- **Inconsistent implementation**: Baltic authorities are considered by business as stricter than other EU states, creating competitive disadvantages.
- **Shifting relationships**: Migration of some business to non-Baltic financial institutions raises concerns about sanctions enforcement.
- **Awareness gaps**: Businesses struggle to keep pace with evolving regulations and highlight the need for better guidance and training.
- **Positive outcomes**: Improved corporate transparency and a deeper understanding of compliance emerged as unintended benefits.

Recommendations:

Based on the survey and the focus group, this report suggests a series of proposals to alleviate the current impact on businesses of sanctions through financial service provision:

- **Proposal 1:** Need for better communication between non-financial businesses, financial institutions, and regulatory authorities.
- **Proposal 2:** Need for a national sanctions policy that addresses the necessity for targeted, practical training and expertise development in sanctions implementation.
- **Proposal 3:** Need for greater harmonization of sanctions implementation within the European Union
- **Proposal 4:** Need for more research and impact assessments

The study concludes that whilst the sanctions are politically necessary, targeted interventions — improved communication, harmonization, and training — can mitigate unintended consequences, ensuring sanctions remain effective, sustainable, and equitable for EU member states.

1. Introduction

Background

Sanctions as a policy tool against aggression have been used increasingly frequently since World War One (Edgar Morgenroth, 2023). Over time, sanctions have evolved, shifting from primarily unilateral actions by individual nations to increasingly collaborative, multilateral efforts led by coalitions, considered more effective and less susceptible to evasion (Sonali Chowdhry et al., 2023). The nature of sanctions has also expanded over time to include specific financial restrictions, personal travel bans, sectoral and industry restrictions, as well as ever greater restrictions to trade.

EU sanctions against Russia and Belarus

Sanctions have become a prominent tool for addressing political challenges, including being one of the main policies collectively actioned by the EU to contain Russian aggression.

The full-scale invasion of Ukraine by Russia in February 2022 was condemned by the majority of the international community, which sought to penalize Russia (and the facilitator of the invasion, Belarus) through a series of increasingly escalating and wide-reaching sanctions. The EU had already imposed "restrictive measures" (henceforth referred to as "sanctions" for simplicity) on Belarus and Russia prior to the invasion. Since 2004, sanctions have been imposed on Belarus in response to growing repression against political opposition, and they were reinforced in 2020 due to increased repression by the Belarusian regime. The EU also implemented sanctions against Russia in March 2014 in response to Russia's unlawful annexation of Crimea and events in eastern Ukraine.

Since 2022, the EU has adopted 15 packages of sanctions against Russia, widely increasing the nature and scope of the sanctions imposed (European Council of the European Union, 2024b, 2024c). They include diplomatic sanctions, such as the suspension of visas, travel bans for state officials and persons related to sanctioned entities, and individuals with a relationship to the state. They also include restrictions on transport and the use of ships and airplanes in European space. The extended sanctions also target industrial sectors with export and import restrictions or outright prohibition of sales (for example, sales of war-related materials or dual-use materials). Also, new measures not previously attempted were introduced to make extended sanctions increasingly comprehensive, such as the provision of a price cap for Russian oil (Meissner & Graziani, 2023). They also target the financial assets of a state, individuals, or companies related to the state, as deemed appropriate. The above also includes the imposition of asset freezes and/or financial restrictions.

Although sanctions within the EU are decided collectively[1], their implementation remains a competence of the member states, and no supranational European authority ensures that the

[1] The European Union reserves the right to impose United Nation sanctions, as well as place its own autonomous sanctions regimes (European Parliamentary Research Service, 2023). The EU imposes sanctions through the Council of the European Union, where the member states are represented. The proposal for sanctions is made by the High Representative of the Union for Foreign Affairs and Security Policy to the Council, where it is discussed by

sanctions are implemented in a homogeneous way. The current sanctions process requires member states to enact their own sanctions law, and national sanctions-enforcing bodies supervise outcomes expected at an EU level.

The EU has introduced a number of initiatives to reduce the variability in sanctions implementation, for example, the creation of an EU sanction-assets task force (Bonifassi et al., 2024) and the EU Directive 2024/1226 (April 2024), which establishes minimum standards for the definition of criminal offenses and penalties related to the violation of sanctions (Official Journal of the European Union, 2024). In addition, a new European authority, the Authority for Anti-Money Laundering (AMLA), was created in June 2024. This authority, although mainly focusing on Anti-Money Laundering standards and supervision, will have a role in sanctions on the financial sector-obliged entities it will directly supervise, but that is expected to commence in 2028 (Authority for Anti-Money Laundering, 2024).

However, **such initiatives can only partially solve the issue of lack of uniformity in sanctions implementation**. There is diversity not only within the EU member states regarding the legal basis of implementing sanctions but also regarding which authority oversees sanctions implementation, as well as the supervision capabilities of each member state.

The imposition of these packages requires a range of responses from the private sector as the list of organizations under sanctions and the type of sanctions imposed are increasing.

The Baltic States at the Forefront of EU Sanctions Efforts

The Baltic states' sanctions regimes

The Baltic states maintain a sanctions regime in line with international and EU standards, covering financial and civil areas, entry restrictions, and control over strategic goods and services. The regime is binding for UN and EU sanctions. Decisions of the Council of the EU on sanctions are implemented in the Baltic states through directly applicable regulations of the EU and the Baltic states’ national legal acts.

Among the Baltic states, only Latvia currently implements national sanctions outside of the EU/UN framework, for instance, those targeting individuals and an entity connected to North Korea's nuclear program (Republic of Latvia, 2017). Lithuania and Estonia, however, do not have an autonomous sanctions list separate from EU or UN frameworks. Table 1 summarizes the main laws and authority in regard to sanctions.

As sanctions against Russia expanded in scope, in April 2024, Latvia undertook legislative changes to enhance the Latvian Financial Intelligence Unit’s role, ensuring it as the national competent authority for sanctions.

In December 2023, the Prime Ministers of Estonia, Latvia, and Lithuania issued a joint declaration (Joint Declaration, 2023). They committed to a unified regional approach to

relevant working parties, thus allowing member states to raise any concerns and make suggestions (European Council of the European Union, 2024a). If agreed, then sanctions, often referred to as sanctions packages, are adopted by the Council of the European Union by unanimity, ensuring that all member state representatives have given tacit approval for the sanctions that are to be implemented.

enhance the implementation of EU sanctions against Russia and Belarus. This collaborative effort was aimed at closing enforcement loopholes and ensuring more effective sanctions, which is crucial given the Baltic States' proximity to Russia and Belarus. The declaration includes a very practical commitment to uniform customs controls and better information exchange to prevent sanctions circumvention, with a deadline set for these measures to be in place by January 31, 2024.

	Estonia	Latvia	Lithuania
Local implementation of sanctions into Law	The International Sanctions Act of 2019	Law on International Sanctions and National Sanctions of the Republic of Latvia of 2016	Law on International Sanctions of 2004
Local competent authority for financial sanctions implementation	Financial Intelligence Unit	Financial Intelligence Unit (Since April 2024)	Financial Crime Investigation Service

SOURCE: (GOVERNMENT OF ESTONIA, 2019; GOVERNMENT OF THE REPUBLIC OF LATVIA, 2024; PORTELA AND OLSEN, 2023; REPUBLIC OF LITHUANIA, 2022)

There is a complex history between Russia (as well as Belarus) and the Baltic states, which, combined with the geographical proximity to both states, resulted in close economic ties, and the Baltic states are thus at the forefront of sanctions efforts of the EU against Russia and Belarus. There is evidence that sanctions decrease economic activity for firms of countries that imposed sanctions, although the overall impact can be limited (Besedes et al., 2021). This cost is proportional to the economic activity of firms in the sanctioned states before sanctions. Typically, the closed Russian business accounted for a significant percentage of a Baltic state's company's overall business, while companies in other EU member states were losing only a small percentage of their overall business.

The Baltic authorities have an increased indirect cost of monitoring sanctions compliance. Latvian authorities have reported a significant uptick in reporting of suspicious transactions or circumventions that align with the increasing severity of sanctions against Russia and Belarus in successive EU sanctions packages, with a 20-fold increase of suspicious transactions reporting related to sanctions and confiscation of more than 3000 shipments to and from Russia and Belarus. By February 2023, prosecuting authorities had launched 121 proceedings, 10 of which had been sent for trial (Portela & Olsen, 2023).

Baltic states also face the practical complexity of differing sanctions regimes between Russia and Belarus. At the time of writing this, around 4,500 products were banned from exporting to Russia, but around 1,500 were banned from exporting to Belarus. These bans cover critical goods like dual-use technologies, advanced machinery, and certain luxury items. Baltic states have reportedly seen an increase in the flow of products permitted into Belarus under sanctions in Russia. Since Russia and Belarus are not subject to the same sanctions regimes, this significantly reduces the effectiveness of the sanctions and introduces greater complexity in enforcing trade sanctions (Financial Intelligence Unit, Latvia, 2024). The Council of the European Union adopted additional sanctions targeting the Belarusian economy on 29th June 2024, aiming to prevent the evasion of sanctions imposed against Russia, given the high degree of economic integration between Russia and Belarus.

Study Framework and Focus

Problem statement

While the effectiveness of sanctions on the countries they are imposed on are frequently studied, research on the impact of sanctions on the sanctioning states is limited. This gap in knowledge hinders authorities ability to make evidence-based decisions and raises the risk that sanctions policies could be impacting business in unintended or disproportionate ways. The lack of research has also been noted by the scientific service of the German parliament, noting that "there are few estimates of the economic impact of sanctions on sanctioning states" (Deutscher Bundestag, 2023). The impact has largely been recorded only in terms of macroeconomic challenges, such as the increase of inflatio and trade interruption, as well as the impact on trade and energy (Darmayadi & Megits, 2023; Reisner, 2023).

The available limited research suggests that businesses are experiencing significant challenges in financial service provision, including increased compliance burdens, transaction delays, and even exclusion from financial systems (Lexis Nexis Risk Solutions, 2023). Specifically for businesses, the effects can include direct effects, such as requiring sanctions compliance in their trade, and indirect effects, such as those arising from business interaction with financial service providers. Because financial institutions are responsible for ensuring their clients' transactions comply with sanctions, they often request additional information. This increases administrative burden for both businesses and financial service providers. Financial service companies in countries that impose sanctions report that business is significantly more challenging and that the complexity of regulations and sanctions environments has imposed restraints on their business engagement.

With the ongoing war in Ukraine, the limited research on the impact of sanctions on EU countries seems to focus on countries experiencing high absolute impact, such as Poland and Germany, rather than the Baltic countries of Latvia, Lithuania, and Estonia, that have borne a high relative cost in terms of their economic welfare (Morgan et al., 2023). With this study, we are making an effort to address the critical gap in evidence and focus on the impact on Baltic business through their financial service provision, which is an under-researched topic.

Research questions

This research aims to spotlight the impact of extended sanctions on an area that is little researched but commonly discussed in the public space: the impact of sanctions on financial service provision for Baltic businesses. The research paper seeks to shed some light on the impact of sanctions on financial service provision to Baltic businesses, focusing on three core questions:

- Do businesses consider that there has been an impact on the financial service provision of Baltic business through the imposition of expanded sanctions against Russia/Belarus?
- In what specific ways businesses and financial providers have been impacted?

- How can that impact be alleviated?

In addition to the above, the exploratory survey and focus group also provided some limited insights into how businesses and financial service providers are striving to stay up to date with sanctions and also seeks to identify practical measures that businesses and financial institutions are taking to adapt to evolving compliance requirements.

Scope of the study

This preliminary investigatory **research focuses on the Baltic states** — Estonia, Latvia, and Lithuania — given their geopolitical context, historical economic interdependencies with Russia, and frontline position in enforcing EU sanctions. The study specifically examines the **challenges Baltic businesses face regarding financial service provision** in the context of the enhanced sanctions of the EU against Russia and Belarus.

These complex issues are difficult to quantify, so we adopted a qualitative, exploratory approach focused on business perspectives. We first conducted an initial survey to identify key issues, then held a focus group with CEOs, compliance professionals, and other stakeholders to gain deeper insights. Our focus is on the effects on businesses and provision of financial services. We do not examine broader macroeconomic impacts.

Significance of the study

This preliminary investigative research addresses a critical gap in understanding the collateral impact of sanctions on the sanctioning states, particularly in financial service provision. By shedding light on the experiences of Baltic businesses and financial institutions, the study aims to provide valuable insights for policymakers, regulators, and financial service providers. Its findings can inform targeted interventions to reduce compliance costs, enhance sanctions enforcement, and improve the ability of businesses to implement sanctions. This study is intended to contribute to open dialogue and enhanced mutual understanding among businesses, state institutions, and financial service providers. Additionally, understanding these impacts can help prevent sanctions fatigue, strengthen public support for sanctions policies, and ensure their long-term effectiveness.

2. Baltic business perspectives on sanctions and financial services: survey and focus group findings

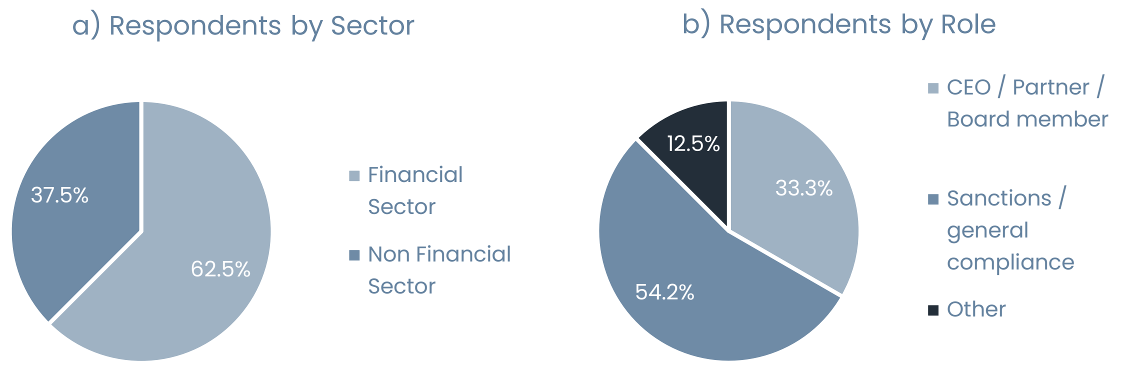
This section presents the results of a survey and focus group exploring the views of Baltic businesses on the impact of sanctions on their businesses and the provision of financial services to those businesses.

Approach to survey and focus group design

The initial intended methodological approach for data collection was based on a survey of businesses across all three Baltic states. A survey covering questions on the impact of sanctions on business practices, costs, and access to and use of financial services was developed and validated with industry experts. To distribute the survey, 21 business and trade associations, as well as 30 other individual businesses, were contacted across the three Baltic states (Latvia, Lithuania, and Estonia). The survey targeted both financial and non-financial businesses.

However, we observed significant reluctance to distribute the survey to members and low response rates from businesses. This hesitancy can partly be attributed to businesses' concerns about engaging and commenting on the adverse effects of sanctions implementation, as discussed in more detail below. Out of the 21 associations contacted, 7 organizations agreed to share the survey with their members (May - July 2024). Overall, the survey received responses from 24 businesses across the three Baltic states (62% from Latvia, 17% from Estonia, and 21% from Lithuania), representing both financial and non-financial sectors.

Figure 1: Descriptive statistics of the explorative survey respondents (N=24)



SOURCE: AUTHOR'S ANALYSIS OF RESPONSES TO THE SURVEY (N=24)

Due to limited engagement and low response rates to the survey, we adapted the research methodology by organizing an anonymous focus group (roundtable) to facilitate an in-depth exploration and discussion of the core themes identified in the exploratory survey.

The focus group discussion took place in September 2024 and included 11 participants from both financial (36%) and non-financial institutions (64%). The non-financial participants represented sectors such as transportation, logistics, medical products, and consumer goods industries. All participants were members of senior management and/or in charge of sanctions compliance.

The majority of the focus group participants were from Latvia. However, several businesses operated across the Baltic states and hence could provide broader comments on sanctions implementation across all three states.

The focus group was conducted under the Chatham House Rule to promote an open discussion. The research team introduced the main questions for discussion, which were followed by a group discussion and an anonymous vote on the core questions. The analysis discussed in this chapter, where appropriate, combines the responses to the survey with the results of the anonymous voting to questions asked during the focus group.

Overall, the focus group approach proved valuable in itself - it allowed participants from financial and non-financial sectors to gain a new understanding of the perspectives and challenges faced by others involved in complying with sanctions. It created a safe space to broach a subject that most businesses find difficult to discuss openly.

Limitations of the research

The research aimed to provide preliminary evidence and successfully broke through the business community's culture of silence on this topic. However, it has limitations that need to be taken into account when interpreting the results.

The results of both the survey and the focus group should be considered as indicative rather than definitive. First, the sample size of the exploratory survey was too small to represent the various business sectors in Latvia, Lithuania, and Estonia affected by sanctions. Instead, the survey served as a tool to refine questions for the focus group discussions. Second, despite efforts to engage businesses across all three Baltic states, the majority of participants were from Latvia. While there was participation from Estonia (13%) and Lithuania (21%) in the survey, the representation was not proportional to the wider business populations in these countries. Additionally, we recognize that businesses willing to discuss the impact of sanctions may be those most affected, introducing a potential reinforcement bias.

Despite these limitations, we believe it is important to publish and discuss the views and experiences of businesses to ensure their voices are heard. Focus group participants highlighted a strong reluctance among companies to share their opinions on this topic, which we discuss in the next section and which partly explains the lack of research in this area. This exploratory research is, therefore, a step in the right direction - only through engagement with stakeholders can the evidence base for better policy design and sanctions implementation be sourced and built.

Core findings from the survey and the focus group

In the sections below, we discuss the core themes arising from both the survey and the focus group, as follows:

- **Theme 1:** Reluctance of business representatives to openly discuss issues around sanctions implementation
- **Theme 2:** The increasingly expanding sanctions have had an effect on businesses and made it more difficult for them to access and use financial services
- **Theme 3:** Differences in sanctions implementation across the EU and non-EU countries can lead to businesses seeking financial services outside of the Baltics or even the EU
- **Theme 4:** Positive impacts from sanctions implementation

Theme 1: Reluctance of business representatives to discuss issues openly around sanctions implementation, including impact on access to financial services

Businesses play an integral role in sanctions enforcement. However, businesses from the Baltic states that participated in the research reported difficulties in finding a meaningful platform to discuss the practical challenges of proportionate sanctions implementation. They are hesitant to voice their struggles due to perceived potential reputational or regulatory consequences and find it challenging to discuss issues while still conveying their support for sanctions overall.[2]

Focus group participants suggested several possible reasons for the lack of discussion on these issues:

- **Decisions about sanctions are largely made at the EU level, and the ability to raise concerns at this level is limited.** Additionally, respondents felt there was very limited scope to influence the design and implementation of sanctions, as they are largely driven by political, not economic considerations.
- **There is a reluctance to take a position that might be construed as criticizing measures that are generally accepted to be politically and morally necessary**. In the Baltics, there is a strong public and political consensus opposing Russian aggression, and businesses worry that drawing attention to their problems could be interpreted as resistance to the sanctions themselves, leading to adverse public reaction. Some suggested that the "culture of silence" is rooted in the history of the Baltic states and the fact that in smaller countries it is difficult to stand out with a dissenting opinion.
- **Businesses may also hesitate to voice concerns about sanctions implementation out of fear of attracting scrutiny from sanction authorities**. Raising such issues could prompt

[2] This was confirmed in the roundtable, when participants required senior level buy-in to participate. It was also conveyed to the research team as a reason why some organisations did not send the initial survey to their members.

authorities to question a company's internal controls, potentially leading to further investigations and additional costs for the business.

- **Raising concerns about sanctions implementation can result in adverse publicity, particularly as sanctions-busting operations are being shut down across Europe**. For example, publicly expressing concerns could coincide with another company being found in violation of sanctions at the same time, leading to reputational damage-by-association.

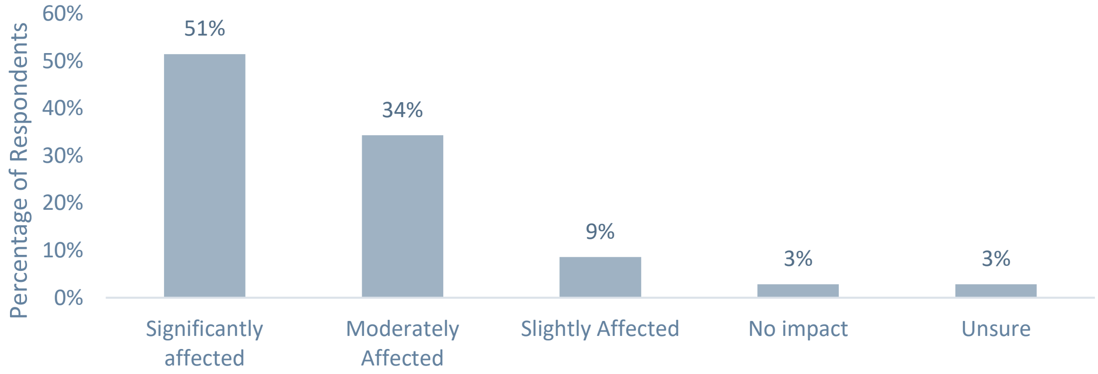
Regardless of the underlying cause, most research participants expressed reluctance to share their views on sanctions publicly, further distancing them from the policymaking and implementation process.

Theme 2: The increasingly expanding sanctions have had an effect on businesses and made it more difficult for them to access and use financial services

The majority (85%) of respondents who participated in the research, either through the survey or the focus group, indicated that sanctions have had a moderate or significant impact on their business (Figure 2). Among survey participants, non-financial business representatives were more likely to report that their business had been significantly affected (71%) than financial service providers (27%).

Respondents noted that the impact is felt across most industries, but particularly in energy, transport, and logistics. Energy and transport businesses must be especially mindful of the European Union's special measures against Russian oil, which are further complicated by the need to comply with the price cap mechanism. This mechanism, which aims to implement a price cap on Russian oil, is complex, and financial service providers face challenges in ensuring compliance, compounded by the risk-averse stance of Baltic regulatory authorities. Overall, representatives from the transport and logistics sectors argued that the complexity of sanctions in these sectors makes financial service providers cautious, often resulting in substantial delays or denials of transaction requests, particularly when financial service providers lack expertise in these business models or transaction types.

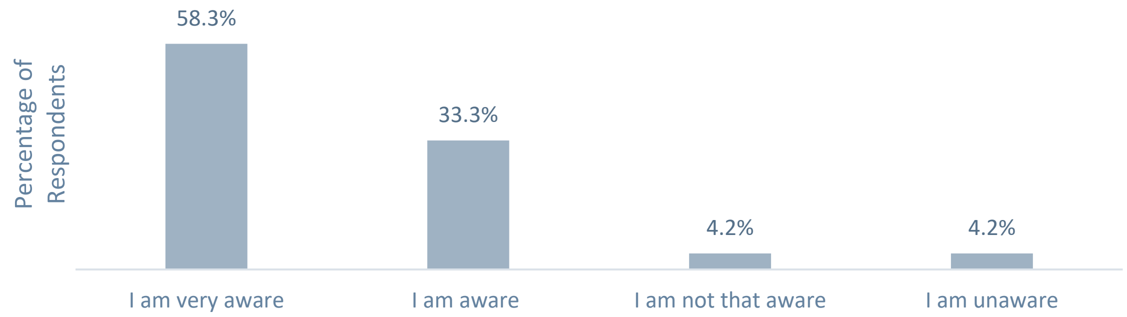
Figure 2: Effect of the enhanced EU sanctions on the survey and focus group participant business (N=35)



Source: Authors' analysis of responses to the survey (N=24) and the focus group discussion (N=11)

The exploratory survey results suggest a high overall awareness of the sanctions currently applied to Russia and Belarus, with 91.6% of respondents indicating they are either "very aware" or "aware" of the extended sanctions (Figure 3). While the sample size is too small to draw definitive conclusions, there appears to be some variation in awareness between non-financial businesses and financial service firms, though both groups operate from a generally high level of awareness.

Figure 3: Awareness of sanctions (N=24)

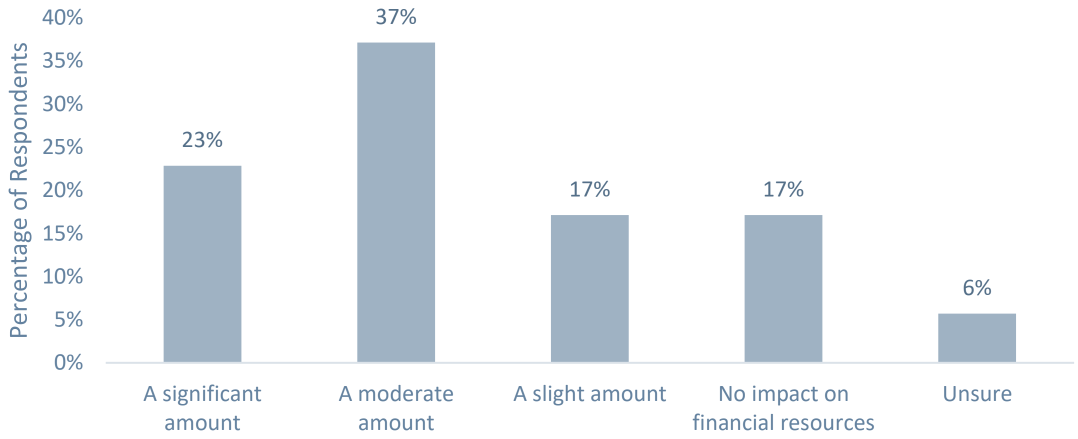


SOURCE: AUTHORS' ANALYSIS OF RESPONSES TO THE SURVEY (N=24)

Overall, 60% of respondents indicated that they have had to allocate moderate to significant financial resources to implement sanctions (Figure 4). While participants were unable to quantify the exact impact, this is an area that warrants further research. Those who reported a moderate or low impact noted that the strain on staff resources is not "overwhelming" but occurs against the backdrop of a challenging economic environment, rising overall costs, and reduced profit margins.

> *"Staff resources that we need to assign to ensure compliance with sanctions are moderate, but these additional requirements come at a time when profit margins are becoming narrower."*
> *- Focus group participant*

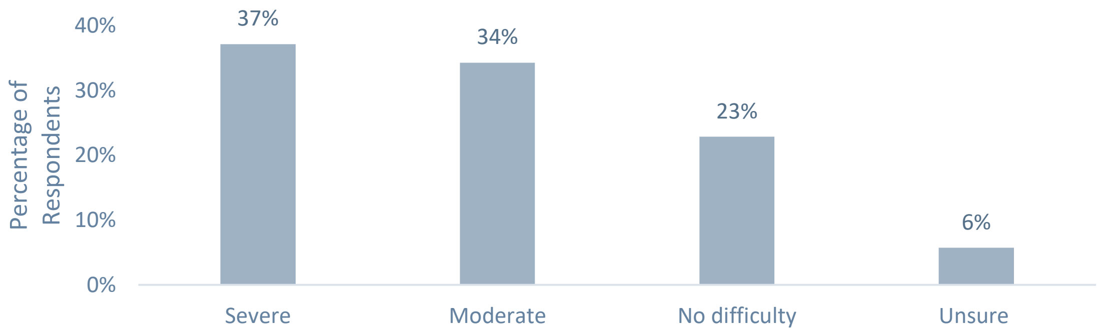
Figure 4: Amount of financial resources used to ensure compliance with the enhanced sanctions(N=35)



SOURCE: AUTHORS ANALYSIS OF RESPONSES TO THE SURVEY (N=24) AND THE FOCUS GROUP DISCUSSION (N=11)

Most research participants (71%) indicated that sanctions had caused "moderate to severe" difficulties in accessing and using financial services (Figure 5). Some noted that financial service provision to businesses was already challenging due to anti-money laundering laws, but the enhanced sanctions have exacerbated the situation. One participant referred to the negative impact on financial services' provision as the "elephant in the room," while others emphasized that this burden is particularly difficult for policymakers to fully understand.

Figure 5: Effect of sanctions on the difficulty of accessing and using financial services (N=35)



SOURCE: AUTHORS ANALYSIS OF RESPONSES TO THE SURVEY (N=24) AND THE FOCUS GROUP DISCUSSION (N=11)

The most commonly reported challenges among research participants were difficulties in conducting financial transactions. For example, survey respondents raised challenges such as an increase in transaction execution time (71% of respondents), reduced availability of services (46% respondents), longer times required to open new accounts (42% respondents), and a rise in the frequency and/or intensity of correspondence with financial institutions (38% respondents).

Additional staff resources must be allocated to meet the demands of financial service providers, such as supplying extra documentation as part of the due diligence process. Respondents noted a significant increase in communication with their banks, with one focus group participant reporting the closure of some bank accounts to manage the burden. Focus group participants highlighted that financial service providers often request documentation in incremental stages rather than all at once, leading to repeated exchanges and delays in the provision of services. Downstream clients, meanwhile, neither understand nor sympathize with these delays and report that other EU countries adopt a far more "business-friendly" approach.

Some remarked that, at times, banks' limited understanding of specific business models or the need to comply with U.S. and other international sanctions can lead to delays and time-consuming repeated exchanges for additional documentation.

"Financial service providers say to us: "bring this document", then come back with a request for another document, and another. It creates uncertainty."
- *Focus group participant*

Overall, focus group participants understood the purpose of sanctions but felt that better communication and understanding with financial service providers and regulatory authorities were needed. Non-financial firms often struggle to understand why certain information is requested, leading to frustration when financial institutions repeatedly ask for additional documentation. Non-financial businesses suggested that providing examples of required information could help reduce compliance costs. However, some financial firms expressed concerns about sharing more information than is strictly necessary, as this could be interpreted as a "tip-off" to businesses, potentially resulting in substantial fines from sanctions or financial authorities.

The issues of communication are at times related to the lack of understanding from banks of the type of business undertaken by some firms. During the focus group, a logistics company shared an example where its financial service provider had asked it to cease all movement of Russian goods, even those permitted under the current sanctions regime, to ensure continued financial service. However, geography presents unavoidable logistical challenges for the Baltic states, as goods originating in Asia often transit through Russia, Iran (with its own sanctions), or the Suez Canal, which poses additional risks. The physical reality of trade means some goods must pass through Russia en route to the Baltics and wider Europe. Financing such trade has become increasingly difficult, with payments often delayed for weeks due to repeated requests for additional documentation from banks, directly causing cash flow issues.

Financial service providers that participated in the research expressed an understanding of their clients' frustrations. In the focus group they noted that factors such as geography, history, and proximity to Russia make financial institutions particularly cautious. This often results in service refusals or delays for business clients, driven in part by extensive bureaucratic back-and-forth in documentation requests, which can cause significant delays.

However, they also felt that the direction is driven by the policies of the sanctions authorities, which they are obligated to follow. As one representative commented, the authorities feel like "we are the beach and the EU is the forest," meaning financial services must err on the side of extreme caution to ensure they are not facilitating sanctions evasion as a gateway to the rest of the EU market. There is a perception by business that Latvia's recent negative track record with anti-money laundering has led authorities to demand that businesses be "cleaner than clean" in implementing sanctions. This stringent approach cascades through the system and affects the provision of financial services to all businesses.

From the banking perspective, the problem, as perceived by business, lies in the vagueness of the regulations, as each EU member state interprets them differently. The Baltic states, perhaps for political reasons, have opted for particularly precise interpretations. Banks are, understandably, being extremely cautious – as the consequences of a mistake can be severe , such as losing a banking license means losing the ability to operate altogether.

> *"As banks, we feel the pressure daily to show the Baltics in a good light by not allowing sanctions evasion. But we also feel that we are reducing the quality of services we provide to our good clients while we try to chase the possible bad actors."*
> *- Focus group participant*

Focus group participants encouraged regulators and policymakers to do more to translate political decisions into practical guidelines. At times, it was felt that the responsibility for determining how to implement specific sanctions was shifted to banks, which then passed it on to their clients, without consideration if the client has sufficient knowledge to adequately respond.

> *"Regulators could do more to translate political decisions into practical actions. Often, they shift the responsibility to the banks, which then pass it on to clients who may not fully understand what the bank expects from them."*
> *- Focus group participant*

Theme 3: Differences in sanctions implementation across EU and non-EU countries can lead businesses to seek financial services outside the Baltics or even outside the EU

A recurring theme in the focus group discussions was the differing approaches of various EU member states. Participants noted that the risk appetite in the Baltic states is generally much lower than in other EU countries due to their proximity to Russia and Belarus, as well as for political reasons, including past AML scandals. They pointed out that other EU financial service providers have a higher risk tolerance when working with firms and regions considered high risk, while Baltic providers avoid such services. Some businesses consider that past money-laundering issues have made authorities extremely concerned about potential political risks. In contrast, other EU states do not prioritize sanctions as highly, allowing their local firms to have less of a sanctions burden, and thus attract clients of Baltic firms.

Businesses operating in multiple countries highlighted instances where banks in Latvia requested more detailed client information than banks in other EU countries, creating inconsistent compliance burdens. A focus group representative of a Latvian non-financial company explained that due diligence regulations require them to ask clients for details about their ultimate beneficial owners to comply with sanctions. However, they are rarely asked for the same information by companies in other EU member states, resulting in a heavier compliance burden compared to businesses in countries with less stringent due diligence processes.

Business in the focus group noted differences in approaches taken by various countries, particularly Spain, France and Germany, in checking transactions for sanctions compliance. One participant argued that in France, banks still review transactions, but the process is quicker, requires less documentation, and has higher thresholds for enhanced due diligence than in Latvia.

> *"Our business, in terms of sanctions compliance, is not asked the same questions that we are required to ask our business partners. Other EU companies do not seem to inquire about that information." - Focus group participant*

Part of that frustration is shared by financial services providers. One company described how onboarding costs have increased and new business is often delayed substantially because of the need to ensure the new business relationship is sanctions compliant. The participant argued that time loss makes them less competitive in the EU market. Overall, there is a culture that errs towards risk aversion from financial service providers. The possibility of an error can lead to a financial service provider facing substantial reputational costs as well as possible financial fines. This makes those responsible within the financial service providers very risk-averse, asking a series of in-depth questions to clients even for very small transactions. A financial service participant noted that a lack of specialised knowledge can lead to additional requests for information, even for relatively safe transactions, ultimately causing execution delays.

Research participants emphasized that unless the current challenges businesses face in accessing and using financial services are addressed, more and more businesses will seek banking and other financial services from other EU providers or even beyond. One focus group participant, for example, noted that their financial transactions were being delayed or blocked in Latvia, so they moved their business to a French bank in Paris that handled transactions without delay. Some participants mentioned knowing of Baltic businesses opening bank accounts in countries outside the EU that do not enforce sanctions. Financial service providers confirmed that they are concerned about this development, and have seem some evidence that clients are seeking their financial services from other EU or non-EU state providers.

The shift of financial intermediaries by Baltic companies poses a challenge for Baltic policymakers and regulators, who are focused on a low-risk, maximum-compliance approach to sanctions. If the current friction in the system is not addressed, businesses may increasingly turn to financial institutions abroad, that are not aligned with Baltic government policies. These foreign institutions would become the main intermediaries for financial transactions, potentially not reflecting the risk preference of the local authorities. In cases where individuals or businesses from Baltic states are involved in sanctions evasion, local authorities would have limited ability to freeze their financial assets, as these transactions would likely occur outside their jurisdiction. As a result, while the reputational damage to the Baltic states would remain, their capacity to combat sanctions evasion effectively would be significantly reduced.

“The money and bank accounts are moving to other countries with a more flexible approach. This is a problem for Baltic countries, not other EU countries. The Baltic states are suffering for being on the frontline of sanctions implementation.”
- Focus group participant

Theme 4: Positive impacts of sanctions implementation

Participants in the survey also identified some positive outcomes, such as an improved understanding of sanctions regulations (42% of survey respondents). For some businesses, the need to comply and report led to a more transparent corporate and ownership structure (29%) was considered a clear benefit to them. Others cited improved communication with their financial service providers as a benefit (29%). Focus group participants also emphasized how the recent experience not only enhanced their sanctions compliance processes but also improved other forms of compliance, including anti-money laundering. Financial service providers in the focus group also identified that they are taking concrete steps to better understand the nature of the business that their clients undertake, which is beneficial in being able to provide them with the right services.

“Through the sanctions compliance required by financial service providers, we have also advanced to the next level in AML/KYC processes."
- Focus group participant

Recommendations

The research conducted is a preliminary assessment of the impact of extended sanctions on business access to financial services. Further research could provide the evidence needed for a tailored policy response. Despite its limitations, the focus group discussed several recommendations to reduce the impact of sanctions on businesses.

Understanding the policy perspective of the Baltic states and the challenges in pushing the European Union toward a more harmonized approach, policymakers should address the issues raised by businesses. In general, businesses have accepted the need to comply, but they are frustrated that compliance has not become easier after more than two years of extended sanctions. Where solutions exist to ensure that financial services are provided to Baltic companies without the issues mentioned, these should be prioritized as a political imperative. Significant efforts are being made on all sides to comply with requirements, but frustration is evident due to the lack of clarity regarding process definitions and the perceived unfairness in the implementation of sanctions compliance in other jurisdictions.

The proposals for necessary improvements fall into four categories:

- **Proposal 1:** Need for better communication between non-financial businesses, financial institutions, and regulatory authorities.
- **Proposal 2:** Need for a national sanctions policy that addresses the necessity for targeted, practical training and expertise development in sanctions implementation.

- **Proposal 3:** Need for greater harmonization of sanctions implementation within the European Union
- **Proposal 4:** Need for more research and impact assessments

Proposal 1: Need for better communication between non-financial businesses, financial institutions, and regulatory authorities

Overall, research participants understood why Baltic state policymakers and sanctions authorities are taking a strong stance in implementing sanctions and why banks are faced with interpreting their implementation in a risk-averse manner. However, after more than two years of extended sanctions against Russia and Belarus, a more open discussion between financial institutions, businesses, and authorities is needed to resolve the current daily obstacles to sanctions implementation in practice.

Generally, stakeholders and businesses wanted greater clarity from banks regarding why certain information is requested and what exactly is needed. Increased transparency about the "behind the scenes" process could eliminate the perception of a presumed "ad-hoc" approach, allowing businesses to respond with less frustration in the future. Some specific suggestions were made, including setting a time limit for the process of requesting evidence and sharing the conclusion of sanitized versions of similar incidents with business, for guidance. .

Financial institutions that participated in the research acknowledged they could improve communication with clients around why an investigation took place following the resolution of the request for evidence.

However, it was not clear who should lead these efforts. Focus group participants argued that it needs to be a "top-down" approach and should not be left to individual financial institutions and businesses. Many issues surrounding the lack of clarity in expectations and communication discussed in the previous sections could be addressed through deeper engagement by the authorities with the affected businesses. Financial institutions argue that it is up to the regulator to lead these efforts to alleviate the burden on businesses, as they will need clear guidance on what alleviation measures would be acceptable to the regulator.

There are positive examples in Anti-Money Laundering that could be emulated. For instance, in the UK, the National Economic Crime Centre (NECC) established the Joint Money Laundering Intelligence Task Force (JIMLIT). This task force consists of over forty financial institutions, financial authorities, and law enforcement agencies. Since 2015, the forum has provided a confidential platform for raising issues, offering guidance, and disseminating information rapidly and proactively. JIMLIT has supported and developed over 950 law enforcement investigations, directly contributing to more than 280 arrests and the seizure of over 86 million pounds sterling. Creating a similar body, particularly in jurisdictions where money laundering and sanctions authorities are unified, could greatly support efforts to combat sanctions evasion and encourage greater cooperation between financial institutions and authorities.

Authorities can also provide more guidance, for example, FAQs or sanitized recent case studies. In addition, a forum for banks and businesses to ask questions and find best practice was also suggested as being a potentially valuable resource.

In general, businesses felt that financial service providers need to adopt a much more risk-based approach when implementing sanctions. Research participants believed there is a need to move away from a "tick-box" and "one-size-fits-all" approach to sanctions compliance by financial institutions. If a firm has demonstrated a proactive and robust approach to compliance and self-policing, and the financial institution has a solid track record with a clear understanding of the firm's trade, it could be added to a "green list" of firms. For these firms, checks by banks or authorities could be lighter or done on a sample basis, rather than the current approach, which involves deep-dive reviews of every transaction. Financial institutions that participated in the research were not opposed to this idea but argued that it is not aligned with the "lowest risk possible" approach that they feel compelled to follow. They would require the regulator's approval and encouragement for such a change in implementation.

The need to understand and listen to business has also been noted by Portela and Olsen who state that the European stakeholders should take more into consideration private actors and business to ensure limited negative intended and unintended consequences of sanctions implementation (Portela and Olsen, 2023; p.52). This should be emulated at a national level by Latvia, Lithuania, and Estonia, as some of the concerns could arise from how the sanctions are implemented locally rather than through EU-level decisions.

Proposal 2: Need for a national sanctions policy that addresses the necessity for targeted, practical training and expertise development in sanctions implementation.

A very significant topic raised by stakeholders was the need for much more training and support in sanctions implementation. All agreed that there is a lack of expertise, or, if that expertise exists, it is not shared in an easily accessible way. Non-financial service companies are being asked to provide all sanctions-relevant information, but their staff members often lack experience, especially in smaller firms. Financial sector businesses are required to comply with an increasing number of complex extended sanctions and must also be aware of sanctions imposed by non-EU countries, such as the US, which can impose extraterritorial penalties.

The business community acknowledges that more training is required for both businesses and financial institutions regarding the implementation of increasingly complex sanctions requirements. The training needed is practical and hands-on, especially in sectors such as transportation, energy, and financial transactions, where sanctions compliance can be quite complex. Research participants felt that existing training is often historical and formal rather than practical and immediately applicable.

Given the policy priority to ensure Baltic states enforce sanctions, policymakers should encourage training and support. Seminars could be provided or subsidized to explain practical considerations. This would not only help companies comply, reducing friction with their financial service providers, but also clarify the need for proper evidence and documentation, which is currently a major source of frustration for businesses. Some businesses also suggested that there is a case for subsidizing capacity building (such as the purchase of software) to support those struggling with the sanctions compliance burden.

Authorities in charge of sanctions can also contribute their expertise by supporting industry-led training and providing sanitized case studies. Published sanitized real case studies have proven to be very useful in Anti-Money Laundering training and are highly valued by financial service firms. Replicating these efforts with sanctions case studies can provide staff with the experience needed to be more effective in complying with the EU sanctions regime.

The joint declaration by Estonia, Latvia, and Lithuania, which ensures the harmonization of customs controls (Joint Declaration, 2023), could be expanded to facilitate the exchange of expertise among financial authorities. Policymakers and authorities in the Baltics could further capitalize on the European Union Peer-to-Peer exchange program to establish direct exchanges that promote greater communication and sharing of expertise. Additionally, other regional initiatives for training and technical assistance could be developed through various EU programs or trilateral state cooperation.

National policymakers can also deploy support from the European Union using the Technical Support Instrument (TSI). This enables member states to design and implement reforms to strengthen governance and can provide knowledge sharing and expertise cooperation related to sanctions.

"Staff training is really needed in a practical way. The need to train will reduce the unfortunate terrorizing of banking clients. Companies feel that the banks expect everyone to be compliance officers, agreed by banks who also say the regulator sometimes comes and does not understand the business. The perspective of the regulator is one that the banks are at fault, with the same mentality as the capital cleaning process."
- Focus group participant

Proposal 3: The need for greater harmonization of sanctions implementation within the European Union

It is important to ensure that the European Union recognizes the need for a greater, Europe-wide effort to achieve uniformity and proportionality in the implementation of sanctions. The current differences in approaches disproportionately affect Baltic businesses compared to those in other EU member states, as highlighted in the box at the end of the section.

Baltic state regulators and policymakers, who have been at the forefront of ensuring the expanded sanctions against Russia are implemented in their member states, could lead the effort to establish a harmonized implementation approach across the European Union. Although some progress has been made on this issue, a discussion should begin on whether sanctions should be an EU-level competency. Since decision-making for sanctions is EU-wide, the implementation system will remain inconsistent if it continues to be a national competency.

A single authority, perhaps as part of the newly created Authority for Anti-Money Laundering, could harmonize sanctions implementation. Even in the short term, a pragmatic approach would be to acknowledge the disproportionate negative impacts during the design phase of a sanction regime and take time to plan mitigation strategies, including mechanisms for redress or redistribution, such as sharing of resources and expertise (Morgan et al., 2023). This mechanism to redress costs could make sanctions coalitions more durable and resilient.

Another way to reduce the negative impact of sanctions on business is for Baltic states to begin a dialogue with other EU member states and allies to ensure that systems are in place well ahead of an event that requires a rapid escalation of sanctions (Portela & Olsen, 2023). This could include preparing for various potential scenarios in which sanctions might be required and assessing the impact of the suggested sanctions on the different EU member states. This planning can take place in advance during the discussion of further rounds of sanctions packages and not just as ad-hoc exercise. Planning and evidence-based sanctions discussion can reduce any negative impact when implemented (Morgan et al., 2023).

Finally, the issue of exterritoriality needs to be addressed. The EU has placed an anti-circumvention framework as part of its 11th sanctions package against Russia. Discussions for further measures indicate that that measure did not fully achieve its purpose. EU member states are asked to implement sanctions, even as third states do not acknowledge them or actively support their evasion. The cost of doing business is rising in the European Union, and the effectiveness of the extended sanctions will be continually compromised unless more efforts are taken to penalize those jurisdictions that profit from sanctions evasion.

Is a pan-European sanctions authority needed?

The financial service business participants in the focus group openly discussed their challenges regarding pan-European attitudes toward sanctions compliance. The two main challenges discussed were:

- The risk appetite varies, with financial service providers in other EU states often mirroring the risk appetite of their respective sanctions authorities.
- The regulation itself is vague and often implemented through national law. The national law can vary in severity and is often unclear, allowing other financial service providers to expect more lax compliance procedures.

The financial service business participants in the focus group noted that, within the spectrum of variability in sanctions implementation across the EU, the Baltic state authorities take the most risk-averse approach. As a result, local financial services must exercise extreme caution to avoid being at fault. They would find it helpful if sanctions authorities provided more detailed explanations regarding their decisions.

The focus group generally wanted to see Baltic policymakers push for a more unified approach to sanctions. Interestingly, the participants did not call for weaker extended sanctions across the EU; rather, they argued that if Europe weakens its borders, it weakens the entire region. However, they would like to see all businesses across the EU held to the same standards when it comes to sanctions implementation.

Such differences in risk appetite and the implementation of EU regulations can only be eliminated through the creation of a pan-European authority. While EU Directive 2024/1126, which established EU-wide rules for defining criminal offenses and penalties related to the violation of EU sanctions, may help reduce variability in implementation across member states (Official Journal of the European Union, 2024), the issue remains that capacity, ability, and risk appetite will continue to vary between EU nations unless sanctions enforcement is standardized at the EU level.

With respect to the European principle of subsidiarity, the enforcement of the extended sanctions requires a pan-European solution to ensure their effective implementation. The new EU Authority for Anti-Money Laundering will provide coordination between anti-money laundering member state authorities. It should also coordinate harmonized sanctions implementation.

Proposal 4: Need for more research and impact assessments

The literature review and feedback from research participants suggest that the impact of sanctions on businesses has not yet been fully assessed from a cost-benefit perspective. There are potential areas where the implementation approach could be improved to reduce unnecessary compliance costs. This applies not only to the Baltic states but also to Europe more broadly. A quantitative impact assessment would help identify ways to make the implementation process more effective and less costly for businesses, without compromising the effectiveness of the sanctions.

3. Conclusion

Academic research on the effects of sanctions on sender nations, particularly the Baltic nations in relation to sanctions against Russia and Belarus, is limited. This exploratory paper provides preliminary evidence from a business perspective and suggests potential policy improvements. Though not definitive, the research underscores the need for further investigation into the impact of sanctions on financial services for businesses.

While the findings are particularly relevant to authorities and firms in the Baltic states, they may also apply to broader EU sanctions implementation.

Overall, financial and non-financial businesses understand the importance of effective sanctions implementation from a political and moral perspective. However, research participants felt hesitant to raise any issues with implementation publicly. Significant efforts are being made on all sides to conform with requirements, but frustration is evident in the lack of clarity with regard to process definition, communication, and perceived unfairness in terms of the implementation of sanctions compliance in other EU and non-EU jurisdictions.

A key area of challenge for the financial institutions, which then creates a downstream challenge for their customers, is the need to conform not only with the direct sanctions requirements but also to recognize the wider regulatory-driven workflows to which they must conform, at risk of severe fines, the threat of extraterritorial-led punishments or even the possibility of losing their banking license. The potential for a severely negative outcome drives a highly risk-averse approach to ensuring sanctions implementation is followed, which can often lead to the bank's customers experiencing a resulting disjointed approach.

Key proposals include the value of improved communication across the business landscape, the need for more training based on real-life examples to foster a better understanding of the involved processes and mitigate roadblocks hindering trade, and a proposal for a pan-European sanctions authority to ensure consistent and balanced sanctions implementation across all EU member states.

Based on direct feedback from businesses, these findings provide a valuable starting point for understanding the effects of sanctions in nations closest to Russia and Belarus. Further research is needed to deepen our understanding of the challenges across different sending countries, ensuring that future planning includes appropriate mitigating measures and leads to more efficient, resilient sanctions implementation.

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