



PARLIAMENTARY ASSEMBLY OF THE MEDITERRANEAN  
ASSEMBLEE PARLEMENTAIRE DE LA MEDITERRANEE  
برلمان البحر الأبيض المتوسط

## Background Information Note

### The Direction of the Russian Federation's Immobilized Foreign Assets to Support Ukraine

*Disclaimer: This document was prepared by the researchers of the International Study Centre of the Parliamentary Assembly of the Mediterranean (PAM) in San Marino, in their personal capacity. The opinions expressed in the note are the authors' own and do not reflect the views of PAM.*

#### Overview

Following the Russian Federation's illegal and unjustified war of aggression against Ukraine in February 2022, the European Union (EU), the Group of Seven nations (G7), and Australia, have frozen a total of 280 billion US dollars of the Central Bank of Russia (CBR), in the form of securities, such as gold and government bonds, and foreign currencies, deposited in their territories. Over two-thirds of this amount, estimated by the EU as 229 billion US dollars, is immobilized in the EU.<sup>1</sup> A smaller portion of Russian assets, amounting to approximately 5 billion US dollars, are frozen by U.S. institutions.<sup>2</sup> It is noted that as of February 2022, Russia's international reserves amounted to 643 billion US dollars.<sup>3</sup>

However, persisting irregularities in the provision of Western financial and especially military support to Ukraine<sup>4</sup>, as well as Russia's further entrenchment in Ukrainian territory and the possibility of a large-scale Russian summer offensive in 2024<sup>5</sup>, the United States (U.S.) and the EU started considering to confiscate and use these assets to the benefit of Ukraine to support its war of liberation and reconstruction projects.<sup>6</sup> In this regard, confiscation refers to the permanent deprivation of CBR assets from Russia with a change of ownership.

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<sup>1</sup> <https://www.reuters.com/world/europe/how-will-west-use-russias-frozen-assets-2024-03-21/>

<sup>2</sup> <https://www.nytimes.com/2023/12/21/us/politics/russian-assets-ukraine.html>

<sup>3</sup> <https://www.consilium.europa.eu/en/policies/sanctions/restrictive-measures-against-russia-over-ukraine/sanctions-against-russia-explained/>

<sup>4</sup> <https://www.theguardian.com/us-news/2024/apr/01/mike-johnson-ukraine-aid>

<sup>5</sup> <https://www.economist.com/leaders/2024/03/27/russia-is-gearing-up-for-a-big-new-push-along-a-long-front-line>

<sup>6</sup> <https://www.nytimes.com/2023/12/21/us/politics/russian-assets-ukraine.html>

Yet, significant doubts remain regarding the conformity of confiscating assets with foreign sovereign immunity under international law, thereby potentially undermining global investor confidence in the eurozone and affecting the credibility of European financial stability.<sup>7</sup>

### **International proposals for action and national positions**

On the path towards the G7 Summit in Italy in June 2024, the U.S. has advocated among G7 members for using immobilized Russian assets to help fund Ukraine's budget needs, and later its reconstruction. This, according to the Secretary of the U.S. Treasury, Ms. Janet Yellen, could be accomplished by seizing the assets or using them as collateral to borrow from global markets.<sup>8</sup>

The plan, reportedly supported by the United Kingdom, Japan, and Canada, is proposed in the composition of three working groups which would "examine the legal issues around confiscation; the method of applying such a policy and mitigating risks; and options for how to best channel the support".<sup>9</sup> In response, Russia stated the possibility of suspending diplomatic relations with the U.S., including the adoption of measures ranging from "asset confiscation to further military escalation", were such action to materialize.<sup>10</sup>

However, Germany, France, and Italy, each member of both the G7 and the EU, expressed reservations regarding confiscation, fearing possible implications on European financial stability and credibility, as well as retaliatory action and litigation from Russia.<sup>11</sup> In this regard, representatives of China, Saudi Arabia, and Indonesia are already reportedly calling privately on the EU to persist against pressure from the U.S. and the United Kingdom urging confiscation.<sup>12</sup>

However, maintaining its will to instrumentalize the funds to the benefit of Ukraine, the second plan, revealed by the EU and expected to materialize soon, is the European Council's February 2024 suggestion to set aside the windfall profits generated by the interest rates placed on the assets, in accordance with EU and international law.<sup>13</sup> The yearly total generated from the interest on these funds is estimated to amount to 3 billion euros, with Belgium already transferring the revenues made from the taxes placed on the interest to Ukraine.<sup>14</sup>

Proposed to the European Commission in March 2024 by Mr. Josep Borrell, EU Vice President and High Representative for Foreign Affairs and Security Policy, this plan aims at allocating

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<sup>7</sup> <https://www.lawfaremedia.org/article/frozen-russian-assets-to-finance-ukraine-collateralization-instead-of-confiscation>

<sup>8</sup> <https://www.bloomberg.com/news/articles/2024-02-29/biden-seeks-plan-to-tap-russian-assets-for-ukraine-by-g-7-summit>

<sup>9</sup> <https://www.ft.com/content/d206baa8-3ec9-42f0-b103-2c098d0486d9>

<sup>10</sup> <https://www.reuters.com/world/russia-diplomatic-ties-with-us-could-break-down-over-asset-seizures-2023-12-22/>

<sup>11</sup> <https://www.ft.com/content/d206baa8-3ec9-42f0-b103-2c098d0486d9>

<sup>12</sup> <https://www.politico.eu/article/russia-frozen-assets-europe-confiscation-china-saudi-arabia/>

<sup>13</sup> <https://www.consilium.europa.eu/en/press/press-releases/2024/02/12/immobilised-russian-assets-council-decides-to-set-aside-extraordinary-revenues/>

<sup>14</sup> [https://www.eeas.europa.eu/delegations/ukraine/ukraine-press-remarks-high-representative-josep-borrell-after-eu-ukraine-association-council\\_en](https://www.eeas.europa.eu/delegations/ukraine/ukraine-press-remarks-high-representative-josep-borrell-after-eu-ukraine-association-council_en)

90% of the aforementioned amount to the European Peace Facility (EPF) to provide military support to Ukraine, with 7% reserved to address Ukraine's reconstruction needs and the strengthening of its defence industry.

Euroclear, a Brussels-based central securities depository, in which the assets in the EU are held and presently immobilized, will reportedly retain the remaining 3% of the profits to cover its operational expenses, or temporarily retain 10% of the profits to cover expected litigation costs if Russia presses legal charges within Belgium. Once the proposal becomes EU law, the generated profits will be paid out twice a year, starting in July 2024.<sup>15</sup>

The last alternative, put forth by the United Kingdom and Belgium in separate proposals, is the collateralization of the immobilized funds to raise and lend money to Ukraine, based on the expectation of their recovery from post-war Russian reparations to be paid to Ukraine. However, collateralization of the funds may likely be subject to the same legal and financial obstacles as total confiscation.<sup>16</sup>

### **Contentious factors**

In contrast to the described proposals for the different uses of immobilized assets, significant obstacles and concerns remain regarding their feasibility and legality.

The greatest contentious element concerning the confiscation of assets, as argued for by the U.S. and its partners, is regarding legality vis-à-vis the established principles of international law, notably the principle of foreign sovereign immunity, as well as each nation's domestic laws. Although central bank assets held in foreign countries are entitled to immunity under customary international law, their immobilization through sanctions under *executive action*, regardless of a judicial proceeding, does not violate immunity. Regardless, Russia has already filed over 100 lawsuits in Russian courts demanding the release of Western assets currently frozen in Russia.

However, measures *changing the ownership* of foreign central bank assets do require judicial action under domestic laws. As such, the introduction of new domestic legislation may allow a national agency to confiscate and avoid an exercise of judicial power and immunity under international law. On this, it should be noted that both international law and domestic constitutional laws may impose limitations on confiscatory measures taken without any form of *prior judicial hearing*, especially in Europe given preceding European Court of Human Rights judgements.<sup>17</sup>

This raises the second most widespread concern regarding the confiscation of CBR assets: As domestic legislation allowing confiscation is widely absent, its introduction would set a precedent and significantly diminish international market confidence in jurisdictions where it

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<sup>15</sup> <https://www.reuters.com/world/europe/how-will-west-use-russias-frozen-assets-2024-03-21/>

<sup>16</sup> <https://www.lawfaremedia.org/article/frozen-russian-assets-to-finance-ukraine-collateralization-instead-of-confiscation>

<sup>17</sup> Brunk, I. (2023) "Central Bank Immunity, Sanctions, and Sovereign Wealth Funds", *George Washington Law Review*, Vanderbilt Law Research Paper 23-12.

would be enabled. Earlier examples of such seizures, including of Iraqi assets after Iraq's 1990 invasion of Kuwait and of German assets after the Second World War, occurred only after their formal conclusion, while the military aggression against Ukraine is still ongoing.<sup>18</sup>

Options related to collateralization of the funds, on the other hand, are tied to the temporary suspension of legal obligations against Russia that are argued to be legally feasible, as long as they urge Russia to pay reparations to Ukraine, as already voted by the UN General Assembly with Resolution A/RES/ES-11/5.<sup>19</sup> In each case, the collateralization of CBR assets is accompanied by varying levels of risk given the uncertain outcome of an ongoing conflict.<sup>20</sup>

## **Conclusion**

Debates regarding the use of immobilized CBR assets to the benefit of Ukraine, as a result of alternative Western financial support to Ukraine, are subject to different sensitive political, legal, and financial variables. In considering these, the West is balancing between the risk of further Russian military aggressions against its members, in case of a Ukrainian defeat, on the one hand and the legal and financial ramifications on European financial stability on the other.

However, the current unfavorable strategic conditions for Ukraine<sup>21</sup> and wavering Western commitment to support Ukraine<sup>22</sup> may cause the materialization of plans beyond the EU's intention to use profits generated from interests, to deliberations of collateralization, or even confiscation.

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<sup>18</sup> <https://www.reuters.com/world/europe/how-will-west-use-russias-frozen-assets-2024-03-21/>

<sup>19</sup> <https://digitallibrary.un.org/record/3994052?ln=en>

<sup>20</sup> <https://www.lawfaremedia.org/article/frozen-russian-assets-to-finance-ukraine-collateralization-instead-of-confiscation>

<sup>21</sup> <https://www.politico.eu/article/ukraine-war-hang-on-in-2024-to-win-in-2025-putin-zelenskyy-russia-counteroffensive/>

<sup>22</sup> <https://www.nytimes.com/2024/04/03/world/europe/nato-ukraine-funding.html>