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HM Treasury

The process for imposing monetary penalties for breaches of financial sanctions:

Consultation response form

Name:
Organisation:
☐ **Please tick if you are responding on behalf an organisation**
Name of organisation (if applicable): N/A
Address:

1. **Do these introductory sections give you enough information to understand the scope of the law on monetary penalties?** ☐ Yes ☒ No

   What else would be useful?

   a. **Section 2.3** – Pursuant to sections 131(3) and (4) of the Policing and Crime Act 2017 (the "**2017 Act**", as reproduced in the draft guidance), the permitted maximum penalty is potentially higher (i.e., in excess of £1,000,000) in cases where a violation of financial sanctions legislation *"relates to particular funds or economic resources and it is possible to estimate the value of the funds or economic resources"*. We understand the reference to *"funds or economic resources"* as intended to relate to breaches of asset freeze sanctions (for example, where funds or economic resources are made available to designated persons). It is unclear whether section 131(3) of the 2017 Act applies to other types of financial sanctions (for example, in respect of dealings with transferable securities or money market instruments issued by, or extensions of credit to, entities listed in the annexes III, V and VI of Council Regulation 833/2014 (as amended)) and, if so, how section 131(3) of the 2017 Act would apply to breaches of these sanctions.

   b. **Section 2.3** – Pursuant to sections 131(3) and (4) of the 2017 Act, the estimated value of funds or economic resources, as the case may be, is central to the determination of the permitted maximum penalty and actual penalty in each case. OFSI should provide guidance as to how it would assess the value of, in particular, goods (falling within the definition of *"economic resources"*). Likewise, OFSI has indicated that in certain circumstances the provision of services to designated persons may be prohibited (see, in particular, paragraph 9.1.10 of the *OFSI Financial Sanctions: Guidance*, dated December 2016). OFSI should provide guidance as to how it would assess the value of such services (or the debt created by such services).

2. What are your views on OFSI's compliance and enforcement approach?

We broadly agree with OFSI's compliance and enforcement approach, in particular, its emphasis on private sector engagement and enabling compliance for its "*customers*", although it is unclear who OFSI's "*customers*" are. We also appreciate the need for OFSI to retain a degree of discretion in its compliance and enforcement approach.

However, in light of the fact that sanctions legislation (including EU Council Regulations) often contains vague or ambiguous terms, it is important that OFSI issue comprehensive guidance upon which persons potentially affected by sanctions legislation can rely.

In addition, OFSI should consider embedding in its approach an expectation that OFSI will regularly seek out and consider feedback from persons affected by sanctions legislation and legal advisers specialised in financial sanctions regarding OFSI's compliance and enforcement approach, and regularly update its guidance to reflect questions repeatedly posed by individual persons and legal advisers.

3. Is there anything else you would expect a compliance model to tackle?

☒ Yes ☐ No

(if yes please explain what below)

OFSI's compliance model includes "*promot[ing] compliance*" through engagement with the private sector and "*enabling compliance*" by providing customers with guidance and alerts to help them discharge their own compliance responsibilities (see **section 2.5.1**). Accordingly, we would expect the model to further address whether OFSI intends to provide guidance on an *ad hoc* or on-going basis and, if so, how and the effect of such guidance on OFSI's case assessment approach and calculation of penalties.

We would also welcome efforts to ensure that OFSI has sufficient resources to address questions from persons potentially affected by sanctions legislation (or their advisors). As discussed at paragraph 5(h)(iv) below, if a person has sought guidance from OFSI and relied on such guidance in good faith, this should be a mitigating factor in any subsequent decision on enforcement or the imposition of a monetary penalty.

4. Do you understand our proposed case assessment approach?

☐ Yes ☒ No

(if no please explain why below)

a. **Section 2.7.2** – The phrase '"*[r]easonable cause to suspect" is a higher standard [than "balance of probabilities"]*' is misleading. The expression "*balance of probabilities*" is the civil standard of proof (contrasting with the criminal standard, "*beyond reasonable doubt*"). The expression "*reasonable cause to suspect*", on the other hand, relates to the mental element that OFSI must conclude exists in order to decide to impose a monetary penalty pursuant to section 131(1) of the 2017 Act. The guidance should not confuse these concepts but rather distinguish between and explain:

   i. the standard of proof applicable for the imposition of monetary penalties under section 131(1) of the 2017 Act; and

   ii. the elements, including the mental element, that must be present for OFSI to decide to impose a monetary penalty.

b. **Section 2.7.4 – The** draft guidance provides that "*an international transaction clearing or transiting through the UK*" will have a "*UK nexus*". For clarity, OFSI should state expressly whether the former phrase encompasses all transactions denominated in Pounds Sterling (and, if not, what types of transaction are excepted).

c. **Section 2.7.4** – The draft guidance provides that "*action by a local subsidiary of a UK parent company*" will

have a "*UK nexus*". This is inconsistent with HM Treasury's guidance on the application of asset freeze sanctions, which states that "*[s]ubsidiaries which are incorporated under EU or UK law must comply with EU and/or UK financial sanctions that are in force, irrespective of where their activities take place*" (emphasis added) (see page 3 of the *OFSI Financial Sanctions: Guidance*, dated December 2016), and standard wording contained in EU Council Regulations regarding their scope of application. OFSI should clarify whether this inconsistency is intentional, and whether non-UK subsidiaries fall within the scope of application of financial sanctions administered by OFSI.

d. **Section 2.7.4** – OFSI should expressly confirm that a "*UK connection*" is satisfied if the conduct in question is by a UK national, irrespective of where the conduct takes place, and the extent to which UK nationals acting as officers of non-UK (or EU) companies could be the subject of enforcement proceedings.

e. **Section 2.7.6** – OFSI should clarify what types of action constitute "*other action short of a penalty*" that OFSI could take in the event that it is unable to impose a monetary penalty. For example, in the United States, the Office of Foreign Assets Control ("**OFAC**") can issue a "*warning*" letter as well as a finding of a violation with no imposition of a penalty.

5. What are your views on our proposed case assessment approach?

a. **Section 2.8** – The draft guidance section on "*case factors*" that can aggravate or mitigate the seriousness of a case from OFSI's perspective is confusing in certain respects. In particular, this section lists discrete offences. In our view, this is inappropriate and confusing. The type of offence involved in a case should not of itself influence the seriousness of a case and, in turn, the possibility of obtaining a reduction in the penalty amount. In the event that OFSI maintains its approach of assessing cases by seriousness, a better approach would be for it to state the factors that would aggravate or mitigate in respect of *each* type of offence.

For completeness, the following "*case factors*" are offences under existing financial sanctions legislation:

i. direct provision of funds or economic resources to a designated person;

ii. circumvention of sanctions;

iii. failure to apply for a licence;

iv. breach of licence terms; and

v. failure to provide information on financial sanctions breaches.

The remaining case factors can be viewed as aggravating / mitigating factors (with the exception of "*public interest, strategic priority and future compliance effect*", discussed at paragraph (g) below).

In addition, the draft guidance refers to various degrees of "*seriousness*" without providing a comprehensive scale of seriousness. It would be helpful if OFSI amended its guidance to do so. For example, the draft guidance states that OFSI will take circumvention of sanctions "*very seriously*" (see **section 2.8 (Circumvention of sanctions)**), whereas it will "*treat a case that directly and openly involves a designated person more seriously than one that is a breach of financial sanctions but does not make funds or economic resources available to a designated person*" (see **section 2.8 (Direct provision of funds or economic resources to a designated person)**).

b. **Section 2.8 (Direct provision of funds or economic resources to a designated person)** – As regards the offences listed in section 2.8, the draft guidance includes a number of qualifying adjectives and adverbs that may be intended to indicate different levels of seriousness. For example, the draft guidance refers to the "*direct*" provision of funds or economic resources to a designated person. It is unclear whether the inclusion of the adjective "*direct*" has any significance, or is intended to contrast with the "*indirect*" provision of funds, for example, to a company owned or controlled by a designated person, where there may be no reasonable cause to suspect that the funds will be transferred to the designated person. This section also states that OFSI "*will normally impose a monetary penalty if the case is not prosecuted criminally*". It is assumed that this statement

relates to any direct provision of funds / economic resources to a designated person, but it is unclear in which circumstances OFSI will consider it inappropriate to impose a monetary penalty.

c. **Section 2.8 (Circumvention of sanctions)** – The definition of "*circumvention*" in the draft guidance is different from the statutory offence (for example, section 10(2) of The Ukraine (European Union Financial Sanctions) (No. 2) Regulations 2014, which provides that "*[a] person commits an offence who intentionally participates in activities knowing that the object or effect of them is (whether directly or indirectly)— (a) to circumvent any of the prohibitions in regulations 3 to 7; or (b) to enable or facilitate the contravention of any such prohibition*"). Since the offence requires a person to have "*intentionally*" participated in certain activities, it is unclear how the fact that they did so "*deliberately*" can be regarded as an aggravating factor. OFSI should either expand on the definition of "*circumvention*" or provide concrete examples, for example, contrasting the situation where a person arranges or structures his affairs to *comply* with financial sanctions, with the situation where a person restructures a transaction (which would otherwise breach sanctions legislation) in order to *avoid* triggering financial sanctions alerts.

d. **Section 2.8 (Severity / Knowledge and compliance standards in the sector)** – OFSI should explain what constitutes "*common due diligence or know-your-customer processes*". For example, in the United States it is common practice for persons to use screening software to ascertain whether they may indirectly be providing resources indirectly to sanctioned entities (denied party screening). OFSI should state whether such a measure would be sufficient for the purpose of conducting due diligence or know-your-customer processes.

   OFSI should also consider the extent to which the nature of the business or industry in which a specific company operates should be taken into account (for example, in many industries sanctions risks may reasonably be considered to be remote and in some businesses, such as those operating from internet platforms, it may be excessively burdensome to require comprehensive screening). OFSI should also consider that in some countries (including countries with elevated sanctions risks) corporate ownership details may not be publicly available with the result that there may be no reliable way to determine the risk of dealing unintentionally with designated persons.

   The draft guidance indicates that OFSI will not seek to punish companies "*when the company has acted swiftly to remedy the cause of the breach*". We consider that such conduct should be identified separately as an important mitigating factor.

e. **Section 2.8 (Behaviour)** – OFSI should clarify what are the "*several broad categories*" of behaviour that OFSI considers reflect compliance in the financial sanctions regime. The draft guidance provides certain examples of what appear to be different types of behaviour. However, it does not make clear whether these examples constitute some (or all) of the stated categories.

f. **Section 2.8 (Reporting of breaches to OFSI)** – OFSI should explain what types of breach "*must*" be reported to it and what powers OFSI would rely upon to compel such reporting. We do not consider that there is a general reporting obligation – which is inconsistent with the concept of "*voluntary*" disclosure – and are therefore of the view that this statement is misleading. Accordingly, other than any discrete obligations, for example, on financial institutions (which should be clearly identified in the guidance), we recommend that OFSI should amend this section to state that it would be "*advisable*" for breaches of financial sanctions to be reported.

   As discussed further at paragraph 7 below, it is important that OFSI clarify the extent to which information provided in voluntary disclosures is:

   i. made available to criminal enforcement authorities or other Government bodies in the UK;

   ii. made available to other competent authorities within the EU (or elsewhere), bearing in mind in particular the fact that many EU Council Regulations impose an obligation on Member States to share information (for example, article 12 of Council Regulation 269/2014 provides that "*[t]he Commission and Member States shall ... share any other relevant information at their disposal in connection with this Regulation ...*"; similarly, article 7(1) of Council Regulation 692/2014 states that "*... the Member States shall ... share any other relevant information at their disposal in connection with this Regulation, in particular information in respect of violation and enforcement problems ...*" and article 7(2) states

that *"[t]he Member States shall immediately inform each other and the Commission of any other relevant information at their disposal which might affect the effective implementation of this regulation"*; meanwhile, article 19 of Council Regulation 2016/44 states that *"Member States and the Commission shall immediately inform each other of the measures taken under this Regulation and shall supply each other with any other relevant information at their disposal in connection with this Regulation, in particular information in respect of violation and enforcement problems ..."*); and

iii. subsequently publicised by OFSI in the context of the imposition of a monetary penalty.

The lack of clear guidance on this may inhibit full disclosures (which OFSI may unfairly consider to constitute an aggravating factor).

g. **Section 2.8 (Public interest, strategic priority and future compliance effect)** – The characterisation of the *"public interest"* as an aggravating / mitigating factor is in our view misplaced. Properly understood, the public interest consideration goes to whether OFSI should proceed with a case *despite* the conclusion of its case assessment. This is recognised in the draft guidance: *"[i]n some instances, even if the facts seem to warrant us imposing a monetary penalty or referring for criminal investigation, we may choose not to do so in the public interest ... In other instances we may choose to take more serious action that the value of the case appears to warrant"*.

h. **Section 2.8 (Other relevant factors)** – OFSI should include the following additional considerations when determining whether to levy a monetary penalty and, if so, what amount that penalty should be.

i. Management Involvement. OFSI should consider the level of management involvement, if any, in the sanctioned conduct. The more remote the behaviour is from management involvement, the less appropriate it is that a monetary penalty be assigned to the company.

ii. Pre-existing Compliance Policy and Procedures. OFSI should consider whether the company has a sanctions compliance policy and procedures. If the sophistication of a company is a consideration that weighs in favour of a monetary penalty, then that company's investment in a pre-existing compliance policy and procedures should act as a counterbalance.

iii. Cooperation. Even in instances where there has been a voluntary disclosure, OFSI should consider the extent to which the company / person has cooperated with the OFSI investigation. OFAC specifically describes cooperation in an investigation as a potential mitigating factor. Companies / persons should be incentivised to cooperate with an investigation.

iv. Good Faith. OFSI should consider whether the company / person has acted in good faith, for example if the company / person has attempted previously to obtain guidance from OFSI about the particular practice at issue. If a company / person has regularly sought out and followed OFSI interpretive guidance, that should be a mitigating factor considered at the penalty phase.

v. Remediation. OFSI should consider the extent to which a company / person has undertaken remedial efforts to prevent recurrence of the sanctions violation. Substantial remediation should be a mitigating factor.

vi. Timing of Violation. OFSI should consider the timing of violation, in particular whether mitigation is appropriate when a violation occurred very shortly after the imposition of a sanction (such as, within a short period after a party was added to a list of designated parties).

vii. Whether a Licence Would Have Been Granted. In cases where a person failed to obtain a licence for a sanctioned practice, OFSI should consider whether, had a licence been sought, the licence would have been granted. If the practice would likely have been licenced, the penalty should be mitigated.

viii. Other Sanctions Enforcement. OFSI should consider the impact of monetary penalties and other sanctions imposed by other regulatory / enforcement agencies on the appropriateness of a penalty. If the company / person has already been subject to monetary penalties or other sanctions

proportionate to the violation, additional sanction may not advance the interests of OFSI's sanctions program.

6. **Does this guidance give you enough information to help you understand how a penalty is calculated?**
☐ Yes ☒ No

(if no please explain why below)

a. **Section 2.11.1** – The draft guidance states that the penalty threshold will be met where a case meets the tests in section 131(1) of the 2017 Act and OFSI assesses it *"to meet the standard for a serious case using the case factors set out at section 2.8"* (notwithstanding that a specific offence has not been committed). This appears to entail a repeat of the case assessment that OFSI would initially have conducted in deciding how to progress the case. In our view, these processes are different and should not involve a repeat of the same considerations; alternatively, if OFSI intends to repeat a review of the same or similar considerations, it should explain how the different processes should be applied.

b. **Section 2.11.6** – OFSI should explain how an *"ordinary reasonable person"* would determine whether a proposed penalty is appropriate to an offence. Absent such explanation, OFSI's decision-making in this regard would be completely opaque. This section (and the draft guidance elsewhere) refers to the *"value of the breach"*. It is unclear how this may be assessed (for example, the application of this concept to breaches of article 5 of Council Regulation 833/2014 (as amended); we also refer generally to our comments in response to **section 2.3**, at paragraph 1(b) above).

c. **Section 2.11.6** – OFSI should expand the guidance in this section to include *"other"* cases in respect of which the permitted maximum is £1,000,000 pursuant to section 131(4) of the 2017 Act. At present, the draft guidance does not make any reference to this type of case, or explain how the matrix at **section 2.11.11** would apply to circumvention offences.

d. **Sections 2.11.13 – 2.11.17** – OFSI should provide further detail about the bases upon which penalties for information offences are imposed and / or calculated. If a person has breached a reporting obligation, it is unclear whether this breach would be remedied entirely by a voluntary disclosure (i.e., by responding to a specific demand for information).

e. **Section 2.11.18** – The draft guidelines note that OFSI *"reserve[s] the right not to impose a penalty in certain circumstances"*. However, the draft guidelines do not make clear how this right differs from OFSI's discretion to discontinue a case as a result of its initial case assessment. OFSI should expand its guidance to explain this difference. In light of the draft guidance read as a whole, it is difficult to envisage a situation whereby OFSI had got to this stage, but then decided not to impose a penalty.

7. **OFSI will reduce the level of penalty if there is voluntary disclosure. What are your views on OFSI's approach to this?**

We generally agree with OFSI's policy of reducing the level of penalty where a person has made a voluntary disclosure. However, the draft guidance provides little detail about how to make a voluntary disclosure and how such disclosure would affect a person's liability in respect of other laws or jurisdictions. For example, the draft guidance vaguely states that OFSI may *"pass details to relevant authorities if this is appropriate and possible under UK law"* (see **section 2.7.5**). Furthermore, a person may be deterred from making voluntary disclosure in circumstances where doing so creates legal risk for him in another jurisdiction (see our comments in response to **section 2.8 (Reporting of breaches to OFSI)**, at paragraph 5(f) above).

The draft guidance also states that OFSI can *"discover"* a party's disclosure to be false or made in bad faith, which could result in a monetary penalty (see **section 2.11.14**). However, the draft guidance is silent about how OFSI would make such a discovery. A person may be deterred from making voluntary disclosure where OFSI has complete discretion to decide whether a party's disclosure is false or in bad faith.

We understand that reductions in penalty amounts are intended to incentivise voluntary disclosure. However,

reductions are also tied to the *"seriousness"* of a case: the draft guidance appears to apply a 50% reduction to *"serious"* cases and a 30% reduction for *"most serious"* cases, without providing any explanation of what cases are *"serious"* as opposed to *"most serious"*. The absence of explanation is confusing and, in our view, this distinction adds a layer of unnecessary complexity. In our view, the *"seriousness"* of an offence is an obvious factor in determining the level of a penalty, and the voluntary disclosure *"reduction"* should be considered separately. We see no need for a higher reduction for less serious offences.

Further, it is not clear from the draft guidance how, or by what measure, cases will be determined to be either *"serious"*, *"most serious"* or so serious as to be referred to criminal investigation agencies (rather than being dealt with by OFSI's civil process). The guidance should make clear where the 'ceiling' for civil disposal lies.

Section 2.11.10 states that the voluntary disclosure reduction applies automatically once the offending person has affirmed that the voluntary disclosure is materially complete. In our view, the guidance should acknowledge and establish a process – common to other voluntary-reporting regimes – that permits persons to file an *"initial"* voluntary disclosure (when sufficient facts are known to make a disclosure to OFSI), followed by a *"final"* voluntary disclosure when the person's investigation of the facts is complete. In our experience, the *"initial"* voluntary disclosure helps the enforcement community because it finds out about a potential issue sooner, while at the same time giving the disclosing party some comfort that it can *"put a marker down"* and work diligently towards preparing a full, accurate and complete final disclosure.

8. Is the process for imposing a penalty and making representations clear from this guidance?

☐ Yes ☒ No

(if no please explain why below)

a. **Section 2.12.1** – This section states that OFSI will *"normally"* inform a person in writing of its intention to impose a monetary penalty. The draft guidance should explain when it will not do so (i.e., what *"normally"* means). Furthermore, given the gravity of a penalty and the possibility that a person will want to make representations in response, we consider that OFSI should be required to provide notice in writing in every case where it imposes a penalty. Such notice should contain the details referred to in **sections 2.12.2 – 2.12.4**, but also, whether OFSI considers the offence to be *"serious"* or *"most serious"* and how OFSI had applied the penalty matrix.

b. **Section 2.12.11** – This section does not adequately set out how OFSI would deal with practical issues that are likely to affect the standard 28-day period within which a person can make written representations to OFSI, for example, delays incurred as a result of a person instructing legal representatives. The draft guidance indicates that the 28-day period runs from the date of the initial letter. It is likely that there may be some delay before this letter is provided by the relevant person within the organisation, and then further delay before persons responsible for the alleged offence are contacted and legal advice obtained. In light of this, it is likely to be unfair if OFSI will not *"normally"* accept late representations, particularly given that new material should not be introduced during the Ministerial review. In our view, OFSI should amend its guidance to ensure a fair and workable system.

9. Do you understand the guidance on seeking a Ministerial review?

☐ Yes ☒ No

Section 2.12.20 – The draft guidance states that the Ministerial review *"will not normally be a way of introducing new material"*. It is unclear what *"normally"* means in this context, and OFSI should set out the circumstances in which a person seeking Ministerial review is able to introduce new material. Moreover, in our view, a person should be able to introduce new material where it is significant and relevant to the case. Absent the ability to do so, there is a greater risk that the Minister's decision will be incorrect and vulnerable to challenge on appeal.

10. What are your views on the process for seeking a Ministerial review?

Section 2.12.22 – OFSI should provide a copy of the report (and any other materials) it prepares for the Minister to the person seeking Ministerial review so as to enable him or her to understand fully the basis of the Minister's

decision and to ensure that the decision-making process is transparent generally. OFSI's report is also likely to be highly relevant to a person in the event that he or she elects to appeal the Minister's decision to the Upper Tribunal.

11. Does this guidance clearly explain why and how OFSI will publish information on penalties imposed for breaches of financial sanctions regulations? ☐ Yes ☒ No

What are your views on the level of information OFSI will publish?

Sections 2.17.1 – 2.17.4 – It is not clear what the term *"normally"* is intended to mean in the context of these sections. We consider that OFSI should adopt a more nuanced approach pursuant to which its decision to publish information and the level of information published is proportionate to the impact that the publication will have on the relevant person. To this end, OFSI may also consider involving affected persons in the drafting of a publication.

Section 2.17.5 – OFSI should clarify what the terms *"normally"* and *"issue"* are intended to mean in the context of this section. In our view, OFSI should not publish any information about a case until any on-going appeals processes are finalised and the possibility of any new appeals processes extinguished. Publication of information prior to that stage may severely and unfairly prejudice an alleged offender.

12. Considering the document as a whole, does this guidance help you clearly understand OFSI's approach to imposing monetary penalties?

Not in relation to the matters set out above. In addition, OFSI should update the guidance's internal cross-references and cross-references to sections of the 2017 Act as necessary.

Please e-mail this form to: OFSIConsultation@hmtreasury.gsi.gov.uk

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