

NOT FOR WIDER DISTRIBUTION

“Non-paper”

**non-paper on the Office of Financial Sanctions Implementation (OFSI) Consultation
on the process of imposing monetary penalties for breaches of financial sanctions**

The observations set out in this paper are intended to set out on an informal basis analysis of both the published consultation document and discussions with OFSI

Principles – OFSI’s compliance and enforcement approach

1. The consultation document has been received as representative of draft guidance for the new monetary penalty regime. OFSI indicate that their compliance and enforcement approach is still at a nascent stage given the ongoing outreach with different sectors and regulated entities. Any such guidance should not discourage information sharing across the industry or indeed between sectors.
2. Combatting financial crime requires co-ordination and co-operation, particularly in the case of financial sanctions where there may be multiple parties to the same breach. The issues raised during discussions with OFSI were the concern that there would be a “race to report” and a reticence to self-incriminate. Whilst OFSI is well placed to facilitate information sharing within the sector and across industries, the current model emphasises individual compliance and singular penalties rather than seeking to adopt positive and negative enforcement of a collective compliance approach. Correspondent relationships demonstrate the necessity of collective compliance as reliance is placed on correspondent to have an effective compliance arrangement in place.

The “consistency challenge” – cross-sector regulation

3. The regulation of financial sanctions poses a unique challenge for OFSI as regulators are commonly defined by the industry over which they supervise. In the imposition of monetary penalties as part of an enhanced enforcement of financial sanctions, OFSI will be expected to administer a fair and proportionate regime which is consistent across disparate industries. Some industries, such as the financial services sector, are heavily regulated whereas others experience a more light-touch approach. As a result, the approach in regulatory oversight will vary depending on the industry involved, and the nature of the compliance arrangements in place.
4. OFSI have emphasised that their aim is to regulate all sectors and is not merely targeted at financial services. Moreover, OFSI clarified that they anticipate individuals and smaller corporate entities with less developed compliance systems and frameworks would form the primary classes of targets for the monetary penalties regime. The guidance document and the monetary penalties regime would benefit from greater clarity on the variance in approach to be adopted across-

NOT FOR WIDER DISTRIBUTION

sectors; to achieve this, case studies from a cross-section of sectors would help establish a coherent compliance approach.

5. The consultation document would benefit from further clarity on how OFSI would apply the new powers across different sectors. Section 2.8 of the Consultation, "Knowledge and compliance standards in the sector", states that there is an expectation to meet regulatory and professional standards. Further guidance is merited as to how OFSI would take compliance arrangements into account, particularly given that for financial services this is the responsibility of the Financial Conduct Authority (FCA).

Systems and controls – the FCA/OFSI dichotomy

6. OFSI have stated that they do not wish to stand in place of the FCA and determine the efficacy of systems and controls. Previous breach report responses from OFSI have required explanations of systems and controls and section 2.5 of the consultation document indicates that as OFSI will "take a holistic approach to ensuring compliance...rather than simply waiting until the law is broken and responding to the breach". a "what good looks like" form of guidance, similar to the FCA's publications on compliance approaches, would benefit in the development of more robust solutions to close gaps which lead to breaches.
7. This would represent a pro-active approach which would also be of benefit to smaller entities both within the sector and beyond. Given that the sector in the jurisdictions in which we operate are subject to tighter scrutiny than other sectors both within the UK and globally, would receive an indirect benefit from a more comprehensive guidance document as other, less regulated industries would be equally informed of the sanctions compliance arrangements that we would be subject to. If our customers are as aware of the sanctions requirements we follow as we are, the cross-sectorial compliance approach may be more easily achieved. We would be able to implement both 'top-down' regulation (via the monetary penalties regime) and 'bottom-up' by requiring the same approach from

Structure and Terminology

8. Care should be taken when applying terminology not used in the Bill. The most prominent example is that the Bill refers to a "breach of a prohibition" or to a "violation". The consultation document by contrast frequently employs the term "offence" which has a different connotation. Linguistics and terminology are deemed particularly important where reputational risk and approach to conduct can have a direct effect on the regulatory status of an institution such as ours. The implications in terminology from one regulator, particularly a "home" regulator, could lead to unexpected and unintended consequences from other regulators, markets and consumers.
9. These unintended consequences can be detrimental to foreign policy objectives as sanctions regimes are lifted. The example of the reaction to the lifting of certain Iranian sanctions demonstrates that changes in the law do not necessarily produce changes in risk appetite decisions, particularly where there is an industry-wide fear of reprisal. A careful balance must be struck not to undermine the flexibility and functionality of financial sanctions as a tool for foreign policy objectives.

Inter-related reporting requirements – OFSI and the NCA

10. The terminology adopted in the consultation document could also lead to a degree of uncertainty in the determination of the relationship with the National Crime Agency (“NCA”). Section 131(1) (s.148 as amended) of the 2017 Bill indicates a civil standard of proof (“on the balance of probabilities”) and section 2.7.13 of the Consultation makes clear that OFSI will refer cases to the National Crime Agency (NCA) in the event that they require a criminal investigation. The consultation document suggests that OFSI will identify when referrals to the NCA are appropriate: “if we think they warrant criminal investigation”; “we will decide...on the facts of each case”; and “the more serious a case, the more likely we are to refer a case”. We would seek further guidance and clarity on how the relationship between OFSI’s civil jurisdiction, the NCA’s criminal jurisdiction and in many ways, the FCA’s regulatory jurisdiction would operate.
11. In the case of _____ where the suspicious activity reporting process necessitates a continuous stream of dialogue and data between banks such as ours and the NCA. _____ have a sophisticated reporting framework behind compliance programmes and the interplay between regulatory and enforcement bodies requires us to understand with whom data is required to be shared. The timeliness of this data reporting may also be key, and in seeking to identify the correct body to share information with, we do not wish to fall foul of non-disclosure penalties by OFSI or other regulators.

Guidance and Case Studies

12. The consultation document would benefit from more practical guidance on how OFSI would employ the new powers conferred by the 2017 Bill. For example, section 150 of the 2017 Bill (as amended) indicates that monetary penalties can be applied to officers of that body for wilful or negligent breaches. Whereas 2.4.3 of the consultation document provides some brief guidance, a greater treatment OFSI’s approach to this power would be helpful.
13. By way of comparison, the FCA’s Senior Managers regime has comparable effects and _____ adopt relevant controls as appropriate. This may include further compliance training, additional internal audit programmes or a different approach to recruitment of relevant staff. Industries not subject to comparable regimes would be at an even greater disadvantage without suitable guidance.
14. As set out, a comparable regulatory regime is the FCA’s oversight over the financial services sector. The FCA frequently publishes details of enforcement actions to form a jurisprudence of its own from which the sector derives both consistency and understanding of their own requirements. Whilst OFSI are under an obligation to publish decisions (section 149 of the 2017 Bill (as amended)), there is no requirement to provide details of the facts. OFSI have stated directly and at industry meetings _____ that publication of the details of such cases may inform those wishing to actively fail to comply with the regime.
15. The same position has been articulated in reference to the use of case studies. The FCA, by way of comparison, publishes examples of “good” and “bad” practice and frequently presents such case studies to the industry to enable regulated persons to determine how best to approach their

NOT FOR WIDER DISTRIBUTION

compliance arrangements. These examples are also used as a method of internal control and are used by internal auditors to benchmark the quality of compliance controls.

16. Section 151 (as amended) of the 2017 Bill requires that guidance must be published as to circumstances which would attract a monetary penalty. urges OFSI to re-consider their position that the use of these would undermine the efficacy of the sanctions regimes by instructing wrong-doers of how to circumvent them. Instead, they would be illustrative to OFSI's regulated persons in helping to inform how breaches can be systemically identified, reported and avoided.