

How deep are your pockets? The UK Treasury consults on financial penalties for breaches of sanctions

9 December 2016

HM Treasury (**HMT**) is being given new powers to impose civil monetary penalties for breaches of financial sanctions. The powers are being introduced from April 2017 as part of a wider programme to increase the penalties for breaching the UK's financial sanctions regime. HMT has just announced a [consultation](#) on its proposed approach to imposing monetary penalties.

These penalties could be imposed on anyone who does business in the UK or where a transaction has a UK nexus (including because funds clear through the UK). Penalties can also be imposed on UK companies or citizens working abroad. Companies should review the consultation and make their views heard by the expiry date of 26 January 2017.

HM Treasury (**HMT**) is being given new powers to impose civil monetary penalties for breaches of financial sanctions. The powers are being introduced from April 2017 as part of a wider programme to increase the penalties for breaching the UK's financial sanctions regime. HMT has just announced a [consultation](#) on its proposed approach to imposing monetary penalties.

These penalties could be imposed on anyone who does business in the UK or where a transaction has a UK nexus (including because funds clear through the UK). Penalties can also be imposed on UK companies or citizens working abroad. Companies should review the consultation and make their views heard by the expiry date of 26 January 2017.

What's changing?

At present, the only penalties for breaching financial sanctions are criminal: fines and prison sentences. (Some regulators can also impose fines for systems and controls failings.) In the 2015 Budget, the Chancellor promised to review the penalties and said that lessons would be learned from the US Office of Foreign Assets Control (**OFAC**).

As part of the Policing and Crime Bill (which is currently going through Parliament), the range of enforcement options will be increased because HMT will acquire the power to impose civil monetary penalties for breaches of financial sanctions. If the breach relates to particular funds or economic resources, the maximum penalty is the greater of £1 million or the estimated value of those funds or economic resources. In all other cases, the maximum penalty is £1 million. In 2016, the most significant breach of financial sanctions was worth around £15 million. This is

likely to result in penalties which are low by OFAC's standards, but given the tiny number of criminal prosecutions in the UK for breaches of sanctions, HMT's new powers are likely to be a significant new enforcement tool.

HMT will be required to issue guidance on the circumstances in which it will impose penalties and how it will determine the amount of the penalty; the consultation is on HMT's draft guidance. HMT proposes to introduce the guidance in April 2017 and will then only review it in March 2018, so the consultation is a key opportunity to give your views on the draft guidance.

When can a penalty be imposed?

The decision to impose a penalty will be taken by the Office of Financial Sanctions Implementation (**OFSI**) within HMT. OFSI will have a range of enforcement tools:

- Issuing enforcement correspondence requiring the recipient to improve its compliance processes;
- Referring a regulated person to their regulator;
- Imposing a civil monetary penalty;
- Referring a case for criminal investigation or prosecution (where the penalty would be imprisonment and/or an unlimited fine); or
- If the breach does not have a UK nexus, referring the case to the relevant authorities in another jurisdiction.

If the Policing and Crime Bill becomes law, OFSI would be able to impose a civil monetary penalty if it is satisfied, on the balance of probabilities, that a person has breached a prohibition or failed to comply with an obligation imposed under financial sanctions legislation and the person knew, or had reasonable cause to suspect, that he/she was in breach of the prohibition or had failed to comply with the obligation. The "balance of probabilities" test is the civil standard of proof and is a significantly easier test to meet than the criminal standard of "beyond reasonable doubt".

A key test will be whether the person had "reasonable cause to suspect" that they were breaching the sanctions. OFSI considers that "reasonable cause to suspect" is not the theoretical possibility that an event might have happened – more is required to establish liability. Instead, "reasonable cause to suspect" covers situations where a person is aware of something that could prompt them to think that the event might have happened. In practice, this test is likely to be difficult to apply, but the key lesson is that if there are circumstances which should put you on notice of a potential breach of sanctions, you cannot turn a blind eye.

If a penalty is imposed on a company, OFSI can also impose a penalty on an officer of the company if it is satisfied that the breach took place with the officer's consent or connivance or was attributable to his/her neglect.

The decision to impose a monetary penalty

OFSI's position is that it will assess each case on its own merits and take a fair and proportionate approach. The guidance sets out aggravating and mitigating factors, as well as situations where OFSI is likely to refer a case for criminal investigation.

Referral for criminal investigation

- Individuals and entities targeted by financial sanctions ("**designated persons**") are publicly listed on OFSI's website. OFSI considers that this list enables anyone to know whether they are dealing with a designated person. As a result, if a case involves making funds or economic resources available to a designated person, in a direct and open way, OFSI will normally impose a monetary penalty if there is no criminal prosecution. (The guidance does not set out the circumstances in which a criminal prosecution will be pursued.)
- Cases involving circumvention will be referred for criminal investigation; if the case is not prosecuted, a monetary penalty will normally be imposed. Circumvention includes deliberately structuring a transaction so as to avoid the impact of financial sanctions or "seeming to comply while deliberately not complying".
- OFSI will also liaise with the National Crime Agency to determine whether a criminal investigation is appropriate in cases where false information has been provided to OFSI or there has been a failure to comply with an order to provide information to OFSI.

Aggravating and mitigating factors

The guidance sets out a number of aggravating and mitigating factors which OFSI will take into account, as follows:

- The value of the funds or economic resources involved in the breach.
- The risk that the breach damaged the objectives of the relevant financial sanctions regime.
- Whether the breach could have been prevented through due diligence or "know your customer" processes.
- Knowledge and compliance standards in the relevant sector. The higher the overall compliance standards, the more serious a breach is likely to be. However, if a company has high standards and has made an error which has been swiftly remedied, this will be a mitigating factor.
- Whether the breach was: deliberate; a mistake; the result of a failure to take reasonable care; a systems and controls failure; the result of a legal error (e.g. misinterpreting the scope of the sanctions); or because the person committing the breach was not aware of their sanctions responsibilities.
- Whether the breach involves professional facilitation (i.e. an individual acting on behalf of or providing advice to a client).
- Whether the breach was a one-off or not. If a breach is repeated, persistent or extended, this will be an aggravating factor.
- Whether enforcement action is in the public interest, for example because the case raises an important point of principle which needs to be tested. On the other hand, if taking action

does not appear to be an appropriate use of enforcement resources, this will be a mitigating factor. (It's not clear whether action taken in other jurisdictions, e.g. the imposition of a significant fine by OFAC, would also be a mitigating factor. However, our view is that the imposition of a significant fine by, for example, OFAC in respect of a breach of US sanctions would not be a mitigating factor if conduct which led to the OFAC fine also amounted to a breach of UK sanctions. This is because OFAC is taking enforcement action under US law and OFSI is taking enforcement action under UK law.)

Voluntary disclosure

Giving voluntary disclosure of a breach is a mitigating factor, whereas failing to do so is an aggravating factor. If several parties are involved in a breach, each party needs to give voluntary disclosure in order to benefit from it (joint disclosure is also acceptable).

The credit available for voluntary disclosure is very significant – 50% in serious cases and up to 30% in the most serious cases. (Note: the guidance refers to credit of "up to 50%" for serious cases in one section and a "50% reduction" elsewhere, so it's not clear whether it is an automatic 50% reduction.)

Credit will only be given for a voluntary disclosure if the person reporting certifies that the report given is materially complete. If the report is incomplete or the disclosure was made in bad faith, this will normally be an aggravating factor and will result in a monetary penalty or criminal investigation. However, credit will not necessarily be lost if the failure to provide information was the result of an error or because new information has emerged.

OFSI's guidance on the timing of any voluntary disclosure is to give disclosure in a timely way and err on the side of early disclosure.

Parties in the regulated sector also need to ensure that they comply with any statutory or regulatory disclosure obligations. Financial institutions are required to provide information to OFSI under some sanctions legislation; failing to do so may result in the imposition of a monetary penalty or a criminal investigation.

The penalty threshold

Under the new guidance, if a case has not been referred for criminal investigation, OFSI will normally impose a penalty if a case involves making funds available to a designated person directly, circumvention, failure to comply with a requirement to give information, or if the case is serious. Penalties may also be imposed for failing to comply with reporting requirements in a licence.

That said, OFSI has discretion not to impose penalties, for example if it is not in the public interest.

The penalty matrix

OFSI will determine a penalty using the following steps:

1. Assessing the maximum penalty which could be imposed;

2. Considering what penalty would be fair and reasonable; this consideration results in the baseline penalty, to which any credit or discount will be applied;
3. Applying any reduction for giving voluntary disclosure; and
4. If there was no voluntary disclosure **and** the case is not "most serious", applying a discount because the case is not "most serious". It is not entirely clear from the guidance when a case will be treated as "most serious", rather than serious.

Baseline penalty, less 50% credit for voluntary disclosure.

Baseline penalty, less potential **discount of up to 15%** because the case is not "most serious".

Baseline penalty, less up to 30% credit for voluntary disclosure.

Full baseline penalty, with no credit given.

It is not clear whether OFSI will treat a single incident which leads to several payments being made to designated persons as one breach or several breaches. If the incident is treated as several breaches, this will increase the overall penalty which is payable, even though the breaches all resulted from the same cause (for example, a problem in the way screening systems have been calibrated). The protection for businesses may lie in the requirement for the penalty to be fair and reasonable – the business would need to argue that a penalty of several million for a single mistake was not reasonable.

Similarly, OFAC provides a penalty matrix in US sanctions regulations, with mitigation available for voluntary disclosure and adverse treatment for more serious or egregious violations of the regulations. OFAC also has the discretion to identify multiple violations of the regulations arising from a single incident, depending on the facts and circumstances.

Challenging a penalty decision

Before imposing a penalty, OFSI will inform a person in writing and explain its reasons for imposing the penalty and the reasoning behind the penalty amount. The recipient will then have 28 days to make representations in writing. This period can be extended, but OFSI will need evidence as to why an extension is reasonable. OFSI will also consider agreeing to a meeting; the written representations must cover any points which the recipient wants to make at the meeting.

OFSI then has 28 days (which can be extended) to consider the written representations and whether to change its proposed approach to the case, before issuing its decision. The recipient has the right to refer the decision for an independent review by a government minister (likely to be the Economic Secretary to the Treasury). OFSI is not involved in the review. Instead, the Minister will review the original materials, any written representations and can take legal advice, before making a fresh decision. The Minister can uphold the OFSI decision, cancel any penalty or change the level of penalty. Any penalty then becomes final and must be paid within 28 days.

If the recipient disagrees with the outcome of the ministerial review, the next stage is to appeal the case to the Upper Tribunal. Again, there is a 28 day time limit for appeals, so any action must

be prompt.

Publicity

As part of its approach to promoting good practice, OFSI will normally publish details of all monetary penalties. Publishing full details might reveal new ways to breach or circumvent sanctions, so OFSI will only publish a summary of the facts, but it will name the person fined. OFSI's summary will also include any compliance lessons.

Other indications of OFSI's approach

The draft guidance also contains some informative nuggets. For example, it states that OFSI construes the sanctions prohibitions widely, and that OFSI takes a holistic approach to ensuring compliance, rather than simply reacting to breaches. Although this is not surprising, it is helpful to see this confirmation.

The draft guidance also states that OFSI may enforce UK sanctions against foreign nationals or companies dealing with UK companies from their home countries, for example because a foreign company has made a payment which is cleared through a UK bank. As currently drafted, the Policing and Crime Bill enables OFSI to impose civil monetary penalties for breaches of UK financial sanctions legislation, but such legislation generally only applies to breaches committed outside the UK if those breaches are committed by UK nationals or companies incorporated in the UK. The basis for OFSI's jurisdiction over foreign companies operating outside the UK may therefore be open to challenge.

If you have questions about compliance with and enforcement of sanctions regulations in the UK, US or other jurisdictions, please let us know.

Contacts



**Lourdes
Catrain**

Partner



Louise Lamb

Partner



Beth Peters

Partner

> [Read the full article online](#)