

Client Update

UK's OFSI to Impose Cash Penalties for Sanctions Violations

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On 1 December 2016, the Office of Financial Sanctions Implementation (“OFSI”) issued a consultation paper on its proposed guidelines for imposing civil penalties for breaches of financial sanctions (the “Consultation Paper”). The consultation stems from OFSI’s new powers of enforcement under the Policing and Crime Bill 2017 (the “2017 Bill”) which is currently passing through Parliament (see our 27 April 2016 client update, [UK Getting More Serious About Sanctions](#)). The proposed measures would radically increase OFSI’s powers to punish entities guilty of breaching financial sanctions, including asset freezes, financial market and services restrictions and fund transfer restrictions.

Historically, there have been few avenues for enforcement of financial sanctions breaches in the UK. HM Revenue and Customs, the UK authority responsible for enforcing trade sanctions and export control breaches, has used civil penalties in the form of “*compound penalties*” as an alternative to prosecution. The UK’s principal regulator of the financial services sector, the Financial Conduct Authority, has levied fines for systems and controls violations in respect of sanctions compliance. OFSI and the entity previously administering financial sanctions, HM Treasury, have not been able to impose civil penalties for financial sanctions and instead have had to rely on criminal prosecution. In practice, very few criminal prosecutions of financial sanctions breaches have been brought.

The Consultation Paper provides valuable insight as to when OFSI will impose civil fines, how their value will be calculated and the types of mitigating and aggravating factors that OFSI will consider. OFSI’s consultation closes on 26 January 2017.

WHEN CAN OFSI USE ITS ENFORCEMENT POWERS?

Under the 2017 Bill, OFSI may impose a civil fine on a person (an entity or individual) if it is satisfied that on the balance of probabilities: (i) the person breached a prohibition or failed to comply with an obligation under financial sanctions legislation; and (ii) the person knew, or had reasonable cause to suspect, that they were in breach (the “Statutory Test”). As noted in our April 2016 update, the “balance of probabilities” threshold of proof is easier to establish than “beyond reasonable doubt”, required to establish criminal liability.

In the Consultation Paper, OFSI clarifies that to take enforcement action, there has to be a connection to the UK, although a person could be liable even if the breach did not occur within UK borders. Examples provided by OFSI of such UK nexus include: an international transaction clearing or transiting through the UK; an overseas subsidiary of a UK parent company involved in a potential violation; and financial products or insurance bought on UK markets, but held or used overseas.

WHAT ENFORCEMENT ACTION WILL OFSI TAKE?

Under the proposed guidelines, once OFSI has been made aware of a breach, it will have four enforcement options (in ascending order of severity): (i) notify a party that it needs to improve its sanctions compliance; (ii) refer any regulated entity to the relevant regulator; (iii) impose a civil fine; and (iv) refer the case for criminal investigation and potential prosecution.

OFSI indicates that it will take a proportionate approach to enforcement by assessing aggravating and mitigating factors. Aggravating factors will include whether: funds or economic resources have been provided directly to a designated person; affairs have been deliberately arranged to avoid triggering sanctions alerts; there has been a failure to apply for a licence; and there have been repeated, persistent or extended breaches. In addition, violations of certain, specific sanctions regimes will be deemed more aggravating than others, based on HM Government’s strategic priorities. OFSI will take into account, on a case-by-case basis, whether it is in the public interest to take particular enforcement action.

Mitigating factors include timely and complete self-disclosure and cooperation with OFSI. The full nature of “cooperation” will presumably fall to be tested before the English courts in due course.

The proposed guidelines state that OFSI will only impose a civil fine where the Statutory Test is met *and* at least one of the following four factors is present:

- The breach resulted in funds or economic resources being made directly available to a person subject to an asset freeze;
- There is evidence of circumvention;
- The case meets the standard of a “serious” breach (this is broadly based on the aggravating factors mentioned above); or
- A person has not complied with the requirement to provide information.

HOW WILL CIVIL FINES BE CALCULATED?

Where OFSI decides to impose a civil fine, it will apply a three stage process to quantify its value.

First, OFSI will determine the statutory maximum penalty it can impose. This will be the greater of £1 million or 50% of the value of the breach. The 2017 Bill defines “*value of the breach*” as the estimated value of the funds or economic resources to which the breach relates.

Second, OFSI will determine the “*baseline penalty*”, which must be considered “*reasonable*” on an objective standard and proportionate to: (i) the value of the breach (if known); and (ii) the extent to which the breach undermined the relevant sanctions regime. At present, it is unclear as to what specific factors will be applied at this stage or their influence on the value of the fine.

Third, OFSI will assess whether a discount should be applied to the baseline penalty.

- If there is **voluntary disclosure**, a 50% discount off the stage two baseline penalty for “*serious*” cases and up to a 30% discount for the “*most serious*” cases applies.
- If there is **no voluntary disclosure** and the case does not fall under the “*most serious*” type, a discount of up to 15% off the baseline penalty applies. If the case is of the “*most serious*” type, no discount applies and the full baseline penalty will apply.

Where a person has also committed an “informational offence” under the relevant sanctions legislation (such as through a person failing to inform OFSI of assets held on behalf of a person subject to an EU asset freeze), OFSI may request the National Crime Agency to bring a criminal prosecution. If no criminal prosecution is brought, OFSI may apply a further monetary penalty.

Once OFSI has determined the penalty, its proposed guidelines state that it will send a letter to the person subject to the penalty setting out the amount of, and reasons for, the fine. There will be 28 calendar days to make written representations to challenge a penalty. If no representations are made in this 28 calendar day period, OFSI will issue a final penalty notice. If representations are made, OFSI will provide a further 28 calendar days in which it will consider and respond to these representations, with OFSI holding discretion to extend this period further if necessary.

A person liable to a penalty may, after making representations to OFSI, seek a review of the decision by a Minister of the Crown who may then (i) uphold the decision and penalty amount; or (ii) uphold the decision and substitute a different amount; or (iii) cancel the decision to impose a penalty. If the Minister decides to uphold the decision, the person can appeal to the Upper Tribunal.

COMPARISON TO OFAC

Both the US Office of Foreign Asset Control (“OFAC”) and OFSI guidelines on civil penalties are based on similar principles and methodologies for calculating monetary penalties. However, the OFAC sanctions enforcement guidelines appear to be more prescriptive and detailed in comparison. When calculating the civil penalty, OFAC pays particular emphasis to wilful or reckless violations of law and awareness of the conduct at issue. OFAC also places a greater emphasis on cooperation where, even if the party does not voluntarily disclose, its base penalty can be reduced by 25-40% for substantial cooperation. In addition, for a “first violation”, the base penalty can be further reduced by up to 25%. There are no indications in the Consultation Paper that the UK authorities intend to apply similar discounts.

The 2017 Bill heralds a stricter UK sanctions enforcement regime. Companies as well as individual officers should be aware of the risks and consequences of sanctions violations. It is critical to ensure ongoing compliance is achieved through necessary licences. The proposed guidelines also highlight the potential benefits of early and full disclosures to the UK authorities and the subsequent importance of cooperation.

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Please do not hesitate to contact us with any questions.