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UK Sanctions Enforcement Update

April 9, 2020

International Trade

On 18 February 2020, the UK Economic Secretary to the Treasury upheld a decision on the part of HM Treasury to impose monetary penalties against Standard Chartered Bank, for breaches of the EU-Russia sanctions and associated UK implementing legislation. The HM Treasury Office of Financial Sanctions Implementation ("OFSI"), which issued the penalties in question, published a notice summarising the enforcement action on 31 March.

The penalties imposed against Standard Chartered total £20.47 million, which represents the largest fine imposed to-date by OFSI under civil enforcement powers that OFSI first obtained in 2017. The Standard Chartered enforcement action is notable in a number of respects, including (1) the fact that this is the first fine in the UK, and one of the first in Europe, for breaches of the EU-Russia sanctions, which were first implemented in 2014; and (2) Standard Chartered's success, both in its negotiations with OFSI and in a subsequent ministerial review process, in reducing the quantum of the penalty.

Underlying Facts

OFSI determined that Standard Chartered had breached Article 5(3) of Council Regulation 833/2014 (the "Regulation"), which prohibits—subject to certain exemptions—UK and EU persons from being part of any arrangement to make new loans or credit available to sanctioned entities, where those loans or credits have a maturity exceeding 30 days.

OFSI's notice concerning the enforcement action states that between 2015 and 2018, Standard Chartered made a series of 102 loans to a majority-owned, non-EU subsidiary of the Russian bank Sberbank, which is designated for sanctions under Article 5 of the Regulation. By virtue of being a majority held, non-EU subsidiary of Sberbank, that subsidiary was subject to the same restrictive measures under Article 5 as Sberbank itself. The OFSI notice states that Standard Chartered had introduced features in its compliance programme enabling loans to sanctioned parties where those loans qualified for an exemption under Article 5(3), which permits loans or credit that have a specific and documented objective of financing the import or export of non-prohibited goods between the EU and any third country. OFSI concluded, however, that 70 of the loan transactions within the scope of its investigation ultimately did not qualify for the exemption in question because those transactions did not have a nexus to imports or exports to or from the EU.

The OFSI Civil Enforcement Regime

OFSI imposed its fine against Standard Chartered through civil enforcement powers first introduced under the UK Policing and Crime Act 2017 ("PACA"). The PACA empowers HM Treasury, through OFSI, to issue monetary penalties for breaches of financial sanctions committed after the PACA came into force (1 April 2017). The legislation provides a maximum civil penalty of the greater of £1,000,000, or 50% of the amount of funds or economic resources at issue in the underlying violation(s).

Before the PACA, breaches of UK financial sanctions were effectively limited to criminal enforcement, and in the case of financial services providers, administrative enforcement by the Financial Conduct Authority ("FCA") under UK financial services legislation. The PACA civil regime introduced a new, and comparatively less burdensome, avenue for UK sanctions enforcement, similar in many respects to the civil enforcement powers held by the U.S. Department of Treasury's Office of Foreign Assets Control under the U.S. sanctions regime.

Following the implementation of the PACA, OFSI published a guidance paper describing the circumstances where it would be appropriate to pursue a civil monetary penalty for sanctions breaches, and how OFSI would determine the amount of the penalty. The OFSI guidance sets forth various general "aggravating" and "mitigating" factors that OFSI will assess in reaching its view as to a baseline penalty, and includes a matrix providing general parameters to guide OFSI in determining whether, and if so by how much, to reduce a fine from the baseline penalty figure. The matrix provides that a baseline penalty can be reduced by 50% where the person provides a prompt and complete voluntary disclosure in a "serious case," and up to 30% for a voluntary disclosure in a "most serious" case.

In the Standard Chartered enforcement action, OFSI determined that the underlying breaches should be considered "most serious," although the penalty notice does not provide significant information as to the underlying facts that drove OFSI's determination. OFSI's enforcement guidelines provide that "'most serious' type cases may involve a very high value, blatant flouting of the law, or severe or lasting damage to the purposes of the sanctions regime." Given that OFSI's penalty notice notes that Standard Chartered "did not wilfully breach the sanctions regime, had acted in good faith, had intended to comply with the relevant restrictions, had fully co-operated with OFSI and had taken remedial steps following the breach," it seems probable that the number and/or value of the underlying transactions giving rise to breaches represented a key focal point in OFSI's "most serious" case determination.

OFSI calculated the penalty amount on the basis of 21 prohibited transactions that occurred after the implementation of the PACA. Those transactions had an estimated value of £97.5 million. OFSI recommended a penalty totalling £31.5 million—a figure amounting to a roughly 35% reduction from the maximum potential fine (assuming that OFSI used the value of the transactions, discounted by 50% under the PACA standards noted above, in forming its baseline penalty). The penalty notice states that the penalty recommendation factored in a 30% reduction on the basis that Standard Chartered had disclosed the suspected breaches to OFSI, carried out an internal investigation, produced a detailed report of their investigation to OFSI, and otherwise cooperated with OFSI. Presumably OFSI also considered those and/or other factors in reducing the baseline penalty from the maximum figure, thus arriving at the £31.5 million total.

The Ministerial Review Process

Standard Chartered exercised its right, under Section 147 of the PACA, to seek ministerial review of the OFSI proposed penalty, through the Economic Secretary to the Treasury. Section 147 of PACA provides that all targets of OFSI penalties are entitled to seek review of the proposed penalty by a Minister of the Crown. During a Section 147 review, the Minister ordinarily will not consider new evidence, but will conduct its review on the basis of the information before OFSI, and can determine to: (i) uphold the OFSI decision to impose a penalty and its amount; (ii) substitute a different amount; or (iii) cancel the decision to impose the penalty.

The Minister determined to uphold OFSI's decision to impose a penalty against Standard Chartered, but to reduce the penalty amount. Although the Minister agreed with OFSI that the breaches by Standard Chartered constituted a "most serious" case, the Minister concluded that OFSI had not given adequate weight to Standard Chartered's cooperation and other mitigating factors (noted above). As a result, the Minister reduced the overall penalties by £11 million.

Standard Chartered accepted the Minister's judgment and did not exercise its right of appeal to the UK Upper Tribunal (a further review option that is provided for in the PACA).

Key Takeaways

The Standard Chartered enforcement action represents the largest fine imposed by OFSI, and the first penalty in the UK under the EU-Russia sanctions. While one must always exercise caution in drawing overarching conclusions from a single enforcement action—particularly given the relatively limited information made available by OFSI in its penalty notices—the Standard Chartered case highlights a number of issues that should be of interest to other companies operating in the UK and EU:

1. **Sanctions Enforcement Risk**: In recent years, there have been expressions in some circles of scepticism over whether the UK and EU authorities would be serious in enforcing sanctions regimes, particularly regimes such as the EU-Russia sanctions that involve major trading partners and associated political considerations. Those voices of scepticism increased in the several years following the PACA, which did not see a large number of OFSI-issued penalties (the Standard Chartered case is only the fourth civil penalty imposed by OFSI, and the first involving a penalty in the millions of GBP[1]).

   The perspective that OFSI has been "light" on enforcement is one that should always, in our judgment, have been approached with caution, particularly given how recently OFSI obtained civil enforcement powers under the PACA. Nevertheless, the Standard Chartered case highlights the ability and willingness of OFSI to use its enforcement powers, including in cases that do not involve wilful conduct and do not involve aspects of the UK/EU sanctions regime that are perceived to carry greater sensitivities from a sanctions policy standpoint (such as, for example, cases involving asset-freezing restrictions, evidence of circumvention, or jurisdictions—such as North Korea, Crimea, and Syria—that are subject to more wide-ranging sanctions regimes).

[1] *See* www.gov.uk/government/collections/enforcement-of-financial-sanctions.

2. **Voluntary Self-Disclosure Considerations:** There are ongoing debates in the UK over the exact circumstances in which UK parties face strict *obligations* to self-disclose sanctions breaches to OFSI and/or other UK regulators or enforcement authorities. It is commonly understood, however, that the scope of sanctions disclosure obligations are greater for UK financial institutions than certain other types of persons and entities. That ultimately may have been one of the factors that motivated Standard Chartered's self-disclosure in its enforcement action.

   For companies that do not face a mandatory self-disclosure obligation, the question of whether or not to submit a *voluntary* self-disclosure to OFSI will be a crucial one, and the Standard Chartered case is noteworthy in this regard. On the one hand, it is apparent from the penalty notice that Standard Chartered's self-disclosure—which OFSI acknowledged, notably, as "voluntary" in nature—was one of the factors that resulted in the mitigation of its penalty, and OFSI's enforcement guidelines clearly emphasise the benefits of voluntary self-disclosure. On the other hand, the Standard Chartered case suggests a potential tendency by OFSI to construe cases as involving "most serious" breaches under their enforcement guidelines even where the facts may not show egregious misconduct. There is nothing, in this regard, on the face of the OFSI penalty notice that suggests that Standard Chartered did not exercise good faith efforts to comply with UK and EU sanctions, and even the number and value of the underlying violations do not seem remarkably high, particularly for a large financial institution that presumably engages in large volumes of loans and other relevant business activities in the ordinary course of its business. If OFSI's perspective on what should be viewed as "serious" or "most serious" proves to encompass a large body of potential voluntary disclosure cases, that could cause many companies to more carefully question whether to make voluntary disclosures to OFSI in the first place.

3. **Risk of Ongoing Violations:** OFSI observed in its penalty notice that the aspects of Standard Chartered's compliance programme allowing loans to sanctioned parties "were not appropriately put in place" and resulted in violations that "persisted over an extended period of time," leading to repeated breaches. That phenomenon—an isolated gap in a compliance programme leading to violations that compound over time—represents a risk for all entities across business sectors, and is something that has exhibited itself in past sanctions and export controls enforcement actions in the UK, other jurisdictions in Europe, and the United States. It emphasises the imperative for companies to develop strategies—taking into consideration risk assessments and reasonable budgeting and resourcing considerations—not only to issue compliance policies and procedures that are structured appropriately, but also to periodically test them to ensure that they are being implemented effectively.

4. **Ministerial Review:** The Standard Chartered case represents the second published case—out of four overall OFSI penalty cases[2]—where the company facing a penalty availed itself of its right to ministerial review, and where the review process resulted in a significant reduction in the ultimate penalty. This suggests that the ministerial review process serves as a meaningful oversight function, and one that could represent a more regular aspect of the PACA enforcement process in UK sanctions cases moving forward.

Our lawyers have substantial experience in assisting clients in UK and EU sanctions enforcement and compliance matters, including matters before OFSI and other UK and European enforcement authorities. If you have any questions concerning this alert or our firm's UK and EU sanctions practice, please contact any of the lawyers below.

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[2] The first being OFSI's September 2019 enforcement action against Telia Carrier UK Ltd. (see https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/842548/Telia_monetary_penalty.pdf).