UK Finance – Written Evidence (BSP0007)

House of Lords EU External Affairs Sub-Committee inquiry into UK sanctions policy after Brexit

1. UK Finance is a trade association representing 300 of the leading firms providing finance, banking and payments-related services in or from the UK. UK Finance has been created by combining the activities of the Asset Based Finance Association, the British Bankers' Association, the Council of Mortgage Lenders, Financial Fraud Action UK, Payments UK and the UK Cards Association.

2. Our members are large and small, national and regional, domestic and international, corporate and mutual, retail and wholesale, physical and virtual, banks and non-banks. Our members' customers are individuals, corporates, charities, clubs, associations and government bodies, served domestically and cross-border. These customers access a wide range of financial and advisory services, essential to their day-to-day activities, from our members. The interests of our members' customers are at the heart of our work.

3. UK Finance is the UK representative on a number of international trade associations including the European Banking Federation and the International Banking Federation

4. We are pleased to respond, as below, to this call for written evidence on the UK's sanctions policy after the UK leaves the EU. At the outset we wish to highlight that UK Finance and our members recognise that decisions' on whether to impose sanctions as a foreign policy and national security tool is a matter for government(s). As such, our response is aimed at informing the viability of implementation to ensure the future application of UK sanctions measures are able to achieve their intended objectives whilst being practical to apply.

5. Our response is intended to set out, on behalf of members, themes which are viewed as particularly important to the overall effectiveness and implementation of the UK's sanctions regime as it moves ahead with developing the legislative framework. In addition, the main points that members would like UK Finance to reinforce are specifically categorised below.

Brexit: UK Sanctions Policy - General Comments

6. **Inter-Linkage with wider Exit Negotiations**: We appreciate that the design of a specific UK sanctions framework will be influenced by the outcome of wider negotiations relating to the UK's withdrawal from the EU. The UK's future ability to interpret sanctions requirements, including those adopted from the EU, will depend on, and must be designed to complement, the strategy/outcome of UK exit negotiations. For instance, equivalence or transitional arrangements post-exit could limit HM Government's ability to interpret UK legislative requirements independently, and it may be necessary to adopt relevant jurisprudence from the European Courts while those arrangements are in place. Equally it is important to give clarity on the ability to rely on previous European case law, guidance and interpretation both during the transition phase and thereafter.

7. **Avoiding EU – UK Sanctions Divergence:** We wish to stress that excessive EU - UK divergence would present financial institutions with considerable practical challenges for compliance, resulting in increased costs and uncertainty for UK based financial institutions and EU institutions with UK exposure.

8. For instance, divergence between EU and UK sanctions (e.g., where there is considered to be sufficient grounds to designate an individual in the EU but not in the UK, or vice versa) would create uncertainty for financial institutions in respect of compliance, and would weaken the overall effectiveness of sanctions implementation. Additionally, where EU designations are imposed, but not replicated by the UK, this could have implications for EU nationals employed by financial institutions (or vice versa re UK nationals working in EU financial institutions) similar to those faced by financial institutions employing US persons.

9. As the UK exit negotiations advance, we would welcome confirmation on whether the jurisprudence of the European Union's courts will continue to be considered once the UK has withdrawn from the EU. For example, would "reasonable grounds to suspect" be interpreted in line with the "sufficiently solid factual basis" interpretation provided by the ECJ? Further, what powers would the European Court of Justice have post-Brexit in relation to EU nationals resident in the UK, especially if there are diverging sanctions requirements?

10. Clarification on the status of ECJ guidance given pre-Brexit to interpretation of UK legislation post-Brexit will be required as well as the influence and weight, if any, of ECJ rulings and EU guidance post-Brexit.

11. **Importance of Defining UK Jurisdictional Scope**: As a result of leaving the EU, businesses operating globally will wish to consider their legal exposure to any new UK sanctions legislation. It is therefore imperative that the UK legislative architecture clearly defines jurisdictional scope as to how wide the net will be cast. The recent HM Government public consultation on the United Kingdom's future legal framework for imposing and implementing sanctions offered a description of the UK's future approach to the extra territorial effect of the enforcement of sanctions.

12. However, our members are of the view that the 'jurisdictional' description in the Government consultation left rather open ended the description of 'UK Jurisdictional Scope'. For example, "a local subsidiary of a UK parent company" would be considered a UK element "depending on the structure of governance". Guidance on what structures of governance would, and would not, introduce a UK element will be required. We feel this will be important in order to give the business and financial community certainty on their legal exposure and related compliance responsibilities.

13. Furthermore, it is important to highlight the US experience, where the de jure reach of US sanctions is extremely broad, and in practice the impact of US sanctions often extend beyond the legal grasp of US authorities. Dozens of major firms have "de-risked" – cutting off customers, licensees, bankers, investors, and even whole lines of business due to, at least in part, perceived direct or indirect sanctions risks. We would not wish either EU or overseas business to withdraw from the UK due to legal extra territorial uncertainty, or for it to impede business reacting to potential future relaxation of a sanctions, where operational complexities associated with unintended consequences force a more cautious commercial approach.

14. **Opportunities to Improve Implementation Effectiveness:** The development of a new legislative and policy framework for sanctions in the UK presents a unique opportunity for the UK to take a more defined position on certain implementation matters. For example, this could include a more implementable description of 'ownership and control'. The current EU guidance, which utilises the concept of control alongside ownership, is viewed by industry as outdated and open to a wide degree of interpretation.

15. A more definitive position on 'ownership and control', perhaps similar to the position taken in the US[1], would greatly assist in the practical application of sanction controls. However, we further

[1] OFAC FAQ 398 at https://www.treasury.gov/resource-center/faqs/Sanctions/Pages/faq_general.aspx#50_percent

recognise that whilst the US approach offers greater legal certainty, its adoption would lead to a UK – EU divergence. As such, we recommend that if the concept of 'control' is to remain, Government should issue definitive guidance on its expectations to how industry should implement this obligation. Whatever approach is adopted the obligation should be for Government to seek to designate entities where it has proof or clearly believes entities are owned or controlled by a designated party.

16. **Improved UK licensing Framework to Enable Permissible Transactions and Ensure UK Competitiveness**: We outline in more detail below a number of areas for how the UK licensing framework could be improved to: a) better enable the processing of permissible transactions into sanctioned environments (i.e., humanitarian transactions into Syria); and b) ensure the future competitiveness of the UK. In addition, HM Government has an opportunity to consider a broader, albeit still limited, licencing regime which also provides for scenarios where funds are required to be transferred for administrative purposes, such as transfers required due to structural reform of a financial institution, which is mandated by statute, or the movement of frozen customer accounts as a result of disposals and acquisitions of entities, particularly financial institutions.

Specific Consultation Questions 1 – 6

Question 1: What advantages and disadvantages does EU membership have for the UK with regard to its approach to sanctions policy?

17. The design of EU sanctions requires the consensus of all 28 individual member states and as such ensures a strong degree of coordination in response to common defence and security threats. EU harmonization is viewed by our members to have heightened the impact of sanctions on designated entities and individuals no matter where in the EU these designated parties are located or access finance services.

18. Moreover, where EU efforts have been coordinated with those of other like minded countries, such as the US, Canada, Australia and Japan the global impact of such measures are far more influential. This has been particularly noted in cases where achieving UN Security Council consensus has been unsuccessful (i.e. in response to Russia's involvement in Eastern Ukraine and the Syrian conflict) or has been more limited in nature (i.e. Iranian sanctions prior to the international nuclear agreement).

19. Globally, a range of regional, sub-regional and unilateral actors have enhanced their utilisation of financial and economic sanctions as a foreign policy and security tool. Consequently, ascertaining how best to comply with increasingly divergent legal and regulatory global sanctions obligations has become a key consideration for many international businesses. For financial institutions with exposure to multiple EU member states the ability to operate under an EU wide sanctions regime is viewed as a major advantage.

20. However, it should also be recognised that implementation and related enforcement of EU sanctions measures falls to individual competent authorities within each member state. This can at times create uneven implementation or variations of what is and isn't permitted by individual member states. The recent ECJ judgment in the Rosneft case and the determination that 'financial assistance' in Article 4(3)(b) of Regulation No. 833/2014 should not be interpreted to include the processing of a payment by a bank or other financial institution is illustrative of EU competent authority divergence.

21. Additionally, securing implementation guidance as to the legal scope of EU sanctions can be a lengthy process with individual member states often reluctant to issue any formal view. This has been particularly evident in the context of Russian sectoral sanctions or other complex scenarios i.e. the processing of humanitarian aid into Syria where there is likely to be some type of engagement of a designated party.

22. Overall, it is worth noting that our members commonly observed that the UK authorities tend to adopt a more cautious interpretation of EU sanction regulations in comparison to their EU counterparts.

Question 2. What is your assessment of the impact on the financial sector that the imposition of sanctions by the UK (separate to the EU) would have, in comparison to its participation in the EU regime, in terms of resources and costs?

23. Until the future UK sanctions framework is defined we are unable to determine relevant resourcing and cost implications. As details become clearer we will happily revert to the Committee with further input. However, at this stage we wish to stress that assessing the impact of a separate UK regime should reflect factors beyond domestic implementation and compliance costs.

24. For instance, the perceived legitimacy in how the UK may impose future sanctions separate to any UN or EU agreement is a complex but important matter for both government and the private sector.

25. The legality of the EU sanctions listing procedures has been an area of recent scrutiny with numerous instances of EU targeted sanctions being challenged within the EU courts. Such challenges can be costly to defend and if lost may result in significant compensation claims. The UK will therefore need to be confident that any future unilateral designations can be defended through the UK courts. Further detail on this issue is provided in paragraphs 57 – 63.

26. For global financial institutions managing diversion of opinion in the legitimacy of non-UN sanctions regimes poses considerable implementation challenges. Unilateral sanctions can also provoke counter-sanctions from target countries. For instance, in 2014, Russia retaliated against Western measures by banning certain imports from the countries that had joined sanctions against Moscow. In late 2015, Russia further retaliated against Turkey with a range of sanctions following the shooting down of a Russian fighter jet by the Turkish air force on the Syria-Turkey border.

27. If the UK were to adopt a more forceful unilateral sanctions policy this may increase the vulnerability of UK banks being targeted by foreign governments through the imposition of retaliation sanctions.

Question 3. What impact might complying with an independent UK sanctions regime have both on UK businesses and on foreign businesses operating in the UK?

28. Determining precise impact is difficult at this stage, however we feel it is worth flagging the following themes which will be relevant for future impact assessment.

Legislating beyond the existing framework

29. On leaving the EU, the UK Government will have a timely opportunity to consider if its interests would be served from legislating for 'the power to impose sanctions regimes for reasons beyond those that the existing framework allows'. For example, "Counter Narcotics Trafficking Sanctions" and "Cyber-related Sanctions" are programmes the US Treasury Office of Foreign Asset Control (OFAC) has at its disposal and HM Government authorities may wish the option to replicate with similar sanctions and associated implantation guidance. A further element Government may wish to consider includes widening

powers to act 'where there is a possibility of flight of funds from other financial crime'.

Enhanced information sharing powers

30. Beyond the current powers provided by EU law, and with the expectation that all of these will be brought across with the European Union (Withdrawal) Bill, HM Government could give consideration to introducing enhanced information sharing powers so that banks and other sectors can share information in a secure environment to improve the effectiveness of sanctions implementation. For example, where a bank identifies an entity which it suspects of involvement in transactions concerning sanctioned persons, an effective means of relaying this information with authorities, and other banks, would assist industry to mitigate engaging in activity with the entity of concern. Equally, the importance of regulatory and government authorities sharing their intelligence with the financial sector should not be underestimated.

UK nexus and related reporting obligations

31. To determine the true impact of an independent sanctions regime it will be critical for the UK nexus from a sanctions perspective to be clearly defined. For example:

- The recent HM Government public consultation on the United Kingdom's future legal framework for imposing and implementing sanctions provides a reference to GBP overseas transactions that clear in the UK. However, it is not clear who may ultimately be held responsible for breaching sanctions under a UK regime, or who has the freezing obligation if, say, a Japanese company pays GBP to a GBP account held at a German bank by a UK designated person and which clears through Bank ABC in UK.

- The legal basis for considering foreign-registered subsidiaries of UK companies to constitute a UK nexus will need to be clarified.

- Financial products brought on the UK markets but held or used overseas.

32. In parallel to defining the UK nexus, we have recommended to HM Government the need to set out a clearer articulation of their intended reporting obligations to be placed on industry, in particular in cases

where the situation does not involve frozen assets, or constitutes a clear sanctions breach, is a rejected payment, or where a firm becomes aware another firm may have breached sanctions.

33. The HM Government public consultation articulates that the new sanctions powers will include reporting obligations, including to report to Government if they know, or suspect, that a current customer, or any customer, in the previous five years, is a sanctioned person. In a number of situations it may be unlikely that a bank will know, or suspect, that it held a customer relationship with a designated person in the previous five years. The only way it could ascertain this, is to undertake a look back over all its closed accounts in the past five years, but if there was no suspicion, or it didn't know, it would not need to do that. In addition, we would question what intelligence could be gathered from a historic relationship which could be up to five years old. Clarity is required on the expectations of reporting (is this a new requirement or will it apply to existing designations)? Where an financial institution becomes aware that a non-customer may have breached sanctions, what approach is expected?

Approaches towards Licensing

34. Our members are of the opinion that the narrow approach of the sanctions related licensing regime in the EU has significant pitfalls. The current EU legal and political landscape means that unintended consequences can arise from a particular sanctions regime that could otherwise be resolved through the introduction of a general licence to address an issue.

35. Our members are clear that the UK's departure from the EU offers an opportunity to create a domestic licensing regime which responds to the sanctions legislation in a comprehensive and coherent way. This is viewed as especially important if the UK wants to remain competitive within international trade and global finance.

36. To be a market leader in this area, the UK authorities should see licences as a key tool to attract legitimate business activity which supports the foreign policy objectives of each sanctions regime.

37. In recognition that UK - EU commercial activity may require multiple licences, consideration should be given to licences required from EU member states, i.e. will the EU be able to grant EU licences for activity in multiple member states and the UK or will licences be required from each EU member state where the activity would otherwise be prohibited?

38. It is our members' view that HM Government should make greater use of general licences to authorise certain activity currently requiring a specific licence. This would have the benefit of reducing some of the strain on the Office of Financial Sanctions Implementation (OFSI) to process applications, and the burden on financial institutions to administrate many specific licences. To support effective implementation we further urge the Government to ensure any new licenses are accompanied by a 'Frequently Asked Questions' document, akin to the current OFAC regime.

39. UK Finance has stressed our willingness to work with HM Government on key areas where the introduction of general licences would maximise the effectiveness of the sanctions regime. But at a minimum the UK should consider greater use of general licences or broader project-based licences for at least transactional related activities (e.g., humanitarian relief activity in otherwise sanctioned territories, or via interaction with otherwise sanctioned governments). In doing so, it is important that general licences or broader project-based licences permit activity by both UK and non-UK persons (and then permit UK institutions to perform activities ordinarily incidental to the permitted/ licensed activity, such as processing a payment for the licensed activity).

40. We would further stress that future general licensing powers should be broad and allow OFSI to issue licences where it is in the public interest to do so. It should avoid the EU approach of publishing narrowly constrained licensing powers.

41. We request that when specific licences are granted for designated persons, OFSI consolidates approved activity into as few licences as practical. Currently, there are instances of designated persons having multiple licences which can cause uncertainty for financial institutions when reviewing transactions for compliance. Greater certainty would be provided by issuing the relevant parties with a new consolidated licence after any change to the approved activities. Consideration could be given to whether the format and currently prescriptive approach to specific licences could be revised (e.g. is specifying remitter and beneficiary account number necessary); this can have a material impact on the timely processing of payments.

42. We suggest that standard bank fees for processing transactions conducted under licences could be incorporated into secondary legislation, to remove the need to request fees to be encompassed when licences are being requested. Alternatively, OFSI could include a standard provision in licences to allow for standard bank fees for transactions authorised by the licence.

43. Historic approaches by the EU that involved pre-authorisation of certain transaction (e.g., A30/30a of Regulation 267/2012 prior to the Joint Comprehensive Plan of Action) has been highly challenging for financial institutions to implement, and we would urge that any similar future framework should be avoided.

44. We recommend thought should be given to a licence database which is easily accessible to registered users seeking to understand whether certain types of activity are lawful or not. Interpretative guidance and enhanced Frequently Asked Questions on the exact nature and scope of provisions contained with sanctions regime should also be used to supplement the need for, and complement general and specific licences.

45. Additionally, an online search system which showed which licences are in place would offer significant benefits to both government and industry. This would not need to hold any confidential information, just the licence number, when it was issued, whether it had been amended, and if it was still valid. This would save substantial time both for industry and HM Government.

46. We suggest that when a licence is amended or revoked, OFSI could inform the parties named in the licence, in particular the relevant financial institutions. This would obviate the need for regular requests to OFSI to confirm that licences are valid and the most up-to-date version. An online licensing system similar to SPIRE would be an improvement, and is an approach that should be explored.

47. Lastly, on ensuring proposed licensing powers are fit for purpose we firmly believe that improvements could be made via legislation (and parallel implementation procedures), that would support the UK to engage effectively in legitimate financial transactions.

Government's proposed additional power to seize funds and assets in order to freeze them

48. The HM Government April White Paper on the UK's future legal framework for imposing and implementing sanctions proposes additional powers to seize funds and assets in order to free them. The White Paper does not offer much detail about how the proposed new powers would operate in practice, and there are important areas where we have recommended further engagement. For example, how would these powers interact with the existing powers under other legislation (not just the Proceeds of Crime Act) to seize funds? Would law

enforcement bodies hold cash or assets that have been seized? Would authorities be requesting that banks hold such assets and if, so how would this be achieved? In the latter case under what obligation would a financial institution be required to receive seized funds/ assets from law enforcement?

49. Moreover, if the financial institution did not already hold a frozen account for the sanctioned party, they would be unlikely to open a new account to receive the frozen funds. Additionally, depending on the asset(s) seized, they may not have the appropriate facility to hold such assets.

50. Any future legislative framework should be clear on the obligations faced by financial institutions who are asked by the authorities to open accounts to hold frozen funds. The Bank of England could be given powers to hold such account.

Question 4. Would you expect there to be a change in the way financial sanctions are enforced in the UK after Brexit and if so, what would be the impact on the UK financial sector? What could be the impact on legal remedies sought in sanctions cases?

51. Given the uncertainty in how future UK sanctions will be applied we are not, at this stage, in a position to determine whether there is likely to be any material change to how sanctions are enforced. As such we have set out below a number of factors that will require clarification and which will impact of related sanctions obligations, including subsequent enforcement.

The need to review non-UN sanctions regimes after a fixed period as well as in response to political developments

52. The future UK sanctions framework would benefit from conducting reviews of non-UN sanctions regimes and individual designations after a set period. Moreover, it is important - and good practice - for regulatory instruments and actions to be reviewed regularly to ensure a fair and equitable approach.

53. All EU regimes include a renewal or sunset provision within them. However, as sanctions regimes have evolved over decades and often in response to dynamic situations, the renewal provisions vary. Most are annual. Interestingly, there are regimes, for example Russia, which have more than one renewal trigger. No doubt the Parliamentary Scrutiny Committees will continue to scrutinise sanctions regimes as they are enacted and renewed.

54. It would be helpful to understand whether the future UK review mechanisms will look at the sanctions regime in its entirety and whether it needs to remain in place or be amended to improve its effectiveness? If a fixed period is to be set, will there be any "trigger events" that would cause a regime to be reviewed prior to the expiry of the fixed period?

55. To advance effective implementation it would be helpful for there to be a consolidation and harmonisation of review provisions. This will go some way to providing legal certainty. As such we would propose that clear guidance and timetabling for renewals (both individual designations and regimes) would be beneficial. In addition, where the sanctions regimes are aligned with the EU ones we have sought confirmation from HM Government on whether it envisages that reviews will take place simultaneously with those in the EU and will these be coordinated.

56. In addition, to ensure sanctions are an effective incentive to change behaviour, there should be an equally robust process for removing sanctions as there is for implementing them. A fixed review period demonstrates to targets that sanctions can be adapted in a timely manner and in response to positive changes in behaviour. We would further highlight that where sanctions are suspended, in comparison to permanently lifted, and therefore may be re-imposed financial institutions are much less confident to re-engage.

Proposed future thresholds for individual designations

57. The proposed threshold as set out in the HM Government April consultation White Paper for individual designations appears neither to lower nor to increase the current legal test of 'reasonable grounds to suspect'. It would seem though that the current threshold is relatively low. As such, the evidence required to substantiate an allegation that an individual or entity has met the designation criteria is not extensive.

58. The argument for maintaining this threshold is a straightforward one. HM Government will have the power to make the case for designations more easily with fewer resources required if the evidential threshold is low. The counter argument though is also a compelling one. If the threshold is low, the quality of data used to identify an individual, or entity designated on a list is poor. This makes compliance harder and more costly. In short, poor data quality makes sanctions less effective. Resources are finite and can be used more intelligently if data quality is improved.

59. By way of example, when a financial institution screens a new designation to identify whether or not a customer relationship is held

and assets may need to be frozen, if the identifying information is wanting e.g., no date of birth, no place of birth, a limited number of aliases, etc., it makes complying with the legislation harder. A bank may be overly cautious and freeze the funds of a person who is not actually the subject of an asset freeze but cannot be discounted, or the institution may not have enough information to identify a genuine target.

60. A solution to this would be to legislate that as a bare minimum the data used should include: addresses, date of birth, all known aliases (including whether strong or weak), etc. Moreover, the legislation should set out clear designation criteria for each sanctions programme, and should mandate the issuing of related guidance from the Office of Sanctions Implementation (OFSI). Where this data is unavailable further dialogue and clarity should be offered to the financial industry on implementation.

Future UK challenge mechanism

61. As an upfront observation we recognise the imperative need to ensure an appropriate balance is struck between applying sanctions and supporting basic legal principles of due process. This does not detract from the importance of sanctions as a foreign policy and security tool but rather stresses that the consequences for a listed entity or individual are extremely serious and as such should, wherever possible, be transparent and open to challenge. Whatever framework is adopted by HM Government, will therefore need to ensure appropriate procedures demonstrate a respect for fundamental rights of defence and effective judicial protection.

62. It is clear that the use of Closed Material Procedures (CMPs) to substantiate allegations and support a designation should greatly assist HM Government defend challenges brought by individuals or entities. However, if there is an over reliance on CMPs, issues may arise with regards to the data quality (and therefore effective implementation of sanctions) used for designations, especially if much of the material used is closed.

63. In view of this, there should be careful consideration of what and how certain identifying information could be disclosed to financial institutions beyond what is available in the public domain, so that effective compliance with the sanctions regime can take place. Perhaps more could be made of confidential lists which could include a provision for information sharing between HM Government and the financial institutions where the disclosure of certain information could pose a threat to national security.

64. Challenges in the EU Courts have been plentiful and largely successful since the case of Kadi. The UK could make more use of 'interim designations' and 'final designations' (as in TAFA 2010), to resolve some of the evidential issues involved in defending challenges to designations.

65. One important power that Parliament could legislate for as part of leaving the EU could be to overcome the confusing dicta of the EU Courts, concerning whether or not evidence can be used to support a designation that was not available at the time the decision to designate was made. For example, if a designation was made on an interim basis and a bank provided significant material about the transactional history, connected parties, cross-jurisdictional activity, etc., of the designated person, at present, the EU General Court would not allow the EU Council to rely on this material to support the designation. A legislative fix in the UK could be applied here to overcome this legal issue. For example, new evidence could be used to support a 'final designation' or similar if it was made available after the 'interim designation'.

66. However the mechanism is taken forward, it is important that once the UK leaves the EU the legislative structure is clear about what happens if a UK designated individual (who is derived from an existing EU designation) wins a challenge in the UK but does not challenge their EU listing (or vice versa). Equally, clarification will be required on whether a person who was designated by both the EU and the UK will have to apply to both to request a review.

67. The UK will further wish to avoid a situation where sanctions are constantly over turned through legal challenge (and then relisting occurs under a different rationale), as frequently happens with EU listings.

Whether future legislation should capture domestic and international terrorist activity as a behaviour that the sanctions powers should target

68. Terrorist activity and other nefarious activity which pose a threat to national security is not limited to UK borders, and therefore proposed legislation as set out in the HM Government consultation is considering powers in the UK which would allow for designations to be made regardless of where the activity has taken place. UK Finance believes this approach would further aid financial institutions to meet their anti-money laundering and counter terrorism financing obligations.

69. In moving forwards clarity will be required on how these proposed legal powers will interact with the powers under the existing terrorism

legislation? What will be achieved over and above the powers in the Terrorism Act, for example? Will the Terrorist Asset Freezing Act 2010, (TAFA) be repealed or would it work alongside the new legislation (which may give rise to the risk of conflicts). Clarity is also required on whether proscribed terrorists will be treated as asset freeze targets as well as how terrorist groups should be treated as opposed to individuals.

70. Where terrorist financing is concerned, this is particularly relevant due to the cross-jurisdictional footprint many terrorists and terrorist groups have. Consequently, the international financial system is vulnerable to facilitating the provision of financial support to individual terrorists and terrorist groups. The ability to address these vulnerabilities would be severely limited if relevant legislation did not include an international dimension.

71. It is understood that the Terrorist Asset Freezing Act 2010, (TAFA) is the existing authority for such sanctions to be imposed. If Government takes the view that TAFA does not bestow the powers necessary to target terrorists, it should consider what changes are required to current legislation, and once set out in sufficient detail, provide a further opportunity for consultation on these.

72. HM Government could determine the extent it considers that terrorism designations by foreign governments can and should be incorporated into the Consolidated List. At minimum, a designation by a foreign government should trigger the UK to consider whether it has sufficient information to add that person to the Consolidated List. The UK government may then wish to align itself more widely with countries in addition to the European Union. Financial institutions have an overarching responsibility to prevent terrorist financing, which would be made easier by more consistent designations across global regulatory authorities.

Question 5. Will the Government need to review its capacity and resources to develop policy on sanctions, and/or to monitor compliance with existing sanctions regimes after Brexit? If so, what is your assessment of staff resources needed in Whitehall, such as in the Foreign and Commonwealth Office, the Department for International Trade, and the Office of Financial Sanctions Enforcement?

73. The use of financial sanctions should not be viewed as cost free to Governments. Effectiveness of sanctions implementation must be based on a good understanding of the legal requirements, as well as

awareness of challenges, difficulties, effects and emerging good practices.

74. As currently structured the machinery of governments often appears ill equipped and resourced to deal with the complexity and demands of sanctions implementation. This is an issue that extends beyond the UK.

75. Balancing the foreign and security objectives of sanctions with the ability of competent government authorities to issue clear guidance and perform licensing functions that ensure the continuation of permissible transactions is essential. As modern sanctions regimes have grown in complexity and increasingly shrouded with legal uncertainty many financial sector actors have chosen, or been left with little option, other than, to 'de-risk'.

76. Accordingly the new framework that the UK will put in place after leaving the EU could offer the opportunity to significantly improve implementation matters; however, this will require suitable expertise, staffing and policy direction.

77. For instance to ensure a clearer framework the UK could take steps to define certain critical terms, which to date have been fraught with uncertainty as to their meaning and scope. Examples include:

- The meaning of 'financial assistance'.
- Clarity over the treatment of money market instruments and transferable securities.
- Entities owned/ controlled by a designated person. We recommend that Government issues guidance do define the concept of 'control' to enhance legal certainty. Moreover, we strongly believe that wherever possible, entities that the authorities believe are owned or controlled by a designated person should be added to the UK Consolidated List.
- Ownership/ control of funds: when does a designated person own/ control funds in the context of payment processing/ correspondent banking? The approach in other EU Member States differs to that set out in the HM Treasury guidance on funds remitted by a designated person from outside the EU.
- Contravention and circumvention will need to be clearly described and defined given their importance for generating civil penalties.

Question 6. What role does the UK's membership in the Financial Action Task Force play with regards to its sanctions policy? Would you expect this to change after Brexit?

78. In practical terms sanctions compliance will need to consider appropriate interaction with other types of compliance related programmes such as anti-money laundering and counter terrorist financing to ensure responsiveness of the measures put in place.

79. In this regard the main interplay between sanctions obligations and those of the Financial Action Task Force (FATF) tend to relate to customer due diligence requirements, monitoring, reporting, risk assessment and implementation of UN sanctions, including international counter terrorism obligations. In 2012 FATF revised its international standards to consolidate an expansion of scope addressing 'targeted financial sanctions related to proliferation'. FATF has further prioritised work on international terrorist organisations, including the Islamic State in Iraq and the Levant (ISIL) which is designated by the UN Security Council in accordance with resolution 1267 (1999).

80. The FATF's work on 'high-risk and non-cooperative jurisdictions' is a further influential factor that can impact on wider sanctions considerations. For instance, in the context of Iranian sanctions easing, UK Finance members have sought to better understand the compliance frameworks (anti-money laundering, counter terrorist financing, anti-corruption) of Iranian banks and the regulatory regime.

81. In considering the UK's engagement in FATF we do not anticipate any significant change occurring as a result of leaving the EU.

The importance of future UK – EU cooperation

82. Our members recognise that the UK is currently a key contributor to shaping the EU's sanctioning practices. It could therefore be assumed that the absence of the UK from EU decision-making may impact on the future willingness of the wider EU membership to build the consensus required for imposing meaningful financial sanctions.

83. Creating a balanced framework that recognises the inter-connected nature of the UK and EU should be a central factor in future

cooperation arrangements. If any significant sanctions implementation spilt were to occur this would have an adverse effect on both UK and EU financial markets. Moreover, differences in sanctions law between the UK and EU would likely impact on wider global correspondent banking relationships and trade finance. In short, lack of UK – EU cooperation will complicate the task of not only creating future sanctions regime but will also make those imposed less viable and influential.

84. As sanctions practices develop and evolve, ensuring UK - EU foreign policy cohesion should remain a central priority. One option for moving forwards could potentially involve some type of decision-making apparatus involving both UK and EU sanctions authorities. The aim, wherever possible, should be to preserve UK - EU harmonised approaches for designing, implementing and enforcing sanctions.

85. Continuing UK – EU interaction will also provide a stronger platform for reducing the divergence of approach with other key actors, notable US sanctioning authorities. As seen in the case of Iranian nuclear sanctions, Cuba and other scenarios a coordinated EU approach involving the UK has offered greater political leverage in situations where EU – US political interests may not always be aligned.

86. In conclusion, our members welcome the opportunity to contribute to this important inquiry and we trust our response helps inform the Committee's thinking. In moving forwards UK Finance remains committed to working with both UK and EU authorities to help advance a broad based understanding on the sanctions implications that may arise once the UK has withdrawn from the EU. As chair of the European Banking Federation sanctions expert group we will continue to explore future options for cooperation with our European counterparts.

87. As ever we stand ready to assist with further deliberations and would be happy to provide further Committee input as required.

20 July 2017