UK Finance evidence to the Foreign Affairs Committee inquiry into Global Britain: the future of UK sanctions policy

UK Finance is the collective voice for the banking and finance industry. Representing more than 250 firms across the industry, we help drive forward positive change to enhance standards, support customers and promote innovation.

We thank the Committee for the opportunity to submit written evidence to its inquiry to explore and evaluate the different options for the UK's approach to sanctions policy after leaving the EU. In preparing this response, we have drawn on the expertise of our well-established sanctions panel of European and international banks. This panel works extensively on mechanisms to improve the effectiveness of sanctions compliance and undertakes significant engagement with EU and US counterparts. At an international level, we have been working closely with the United Nations, the EU and UK Government officials on a range of sanctions implementation matters, such as: the impact of the US withdrawal from the Joint Comprehensive Plan of Action (JCPOA), US specific sanctions on Russia, humanitarian issues and mitigating the risk of North Korean sanctions evasion. Furthermore, we provide expert input into a number of international groupings and currently chair the European Banking Federation Sanctions Expert Group.

Additionally, our members have worked closely on the introduction of the Sanctions and Anti-Money Laundering Act 2018 (SAML) which industry views as a necessary piece of legislation to ensure the Government is equipped to implement its foreign policy and national security priorities following Brexit. In considering the Act's implementation, of crucial importance will be how the UK will approach sanctions and utilise the broad powers at its disposal post-Brexit.

In support of this, we have been actively engaged on all aspects of the Act's legislative trajectory. We responded to the Foreign and Commonwealth Office Sanctions White Paper, submitted written evidence to the recent House of Lords EU External Affairs Sub-Committee inquiry on sanctions, published a Parliamentary briefing on the impact of Brexit on sanctions, held a well-received roundtable in Westminster and provided bilateral briefings to MPs and peers.

We further recognise that operating outside the current EU framework will enable, and may somewhat necessitate, a greater flexibility in the design of sanctions programmes. As such, the UK should ensure it is at the forefront of offering a visionary and 'fit for purpose' view on the application of sanctions in what can only be described as a highly complex geopolitical environment.

In submitting this detailed response to the inquiry's terms of reference, we wish to highlight that decisions on whether to apply sanctions is a matter for government(s). Therefore, our intention with this submission is to assist the Committee's deliberations on key factors that should be considered to ensure maximum implementation effectiveness of future UK sanctions.

The effectiveness of sanctions as an instrument of foreign policy, including examples of both successful and unsuccessful use of sanctions to influence the behaviour of foreign actors.

It is imperative that the future effectiveness of the UK sanctions regime is viewed within the wider international geopolitical context. Recent years have seen an unprecedented growth of the use of sanctions and innovation in the types of sanctions applied. Financial sanctions now play a greater role than ever before in foreign policy. As such our members believe it is essential that the UK is at the forefront of policy

development, offering a visionary and 'fit for purpose' view on the application of sanctions in what can only be described as a highly complex geo-political environment.

The international sanctions compliance and enforcement landscape in which our members operate is changing faster than ever before. The past 18 months has seen increased international sanctions pressure on Syria, and North Korea, continued concern over terrorist groups, increased US sanctions on Iran, Russia and Venezuela and the roll back of Cuban sanctions relief provided under President Obama. US Congress activity has been a notable factor within this and has included the codifying and strengthening of existing sanctions measures against Russia, Iran and North Korea by passing in August 2017 the unprecedented "Countering America's Adversaries through Sanctions Act" ("CAATSA").

Our members' view that the growing international reliance on sanctions as the 'go to' instrument of coercion, plus the increasing growth of retaliatory counter measures, will continue to shape our operating environment. In response to such divergent requirements, global banks have increasingly committed to complying with the sanctions laws and regulations of the UN, EU and US plus jurisdictions in which they operate. In this regard, banks set global sanction policies that define minimum standards for compliance across the group. As such, because these banks comply with all applicable sanctions, it may go against their global policy to undertake business that would not be permitted in other jurisdictions (e.g, the US) but would be permitted, or even encouraged, by the UK.

Consequently, given the breadth of UK Finance membership, each bank's approach to the sanctions and franchise risk will be influenced by a range of factors, and for this reason, the appetite for each bank to engage in certain activities or within jurisdictions, subject to some level of non-UK sanctions, may vary considerably.

We further note that differing geopolitical interests and viewpoints are increasingly impacting global cooperation. For instance, the growing transatlantic US-EU digression of sanctions approach toward Iran has resulted in global financial institutions having to ascertain how best to comply with progressively conflicting legal and regulatory sanctions obligations. The August 2018 expansion of the scope of the EU Blocking Regulation to protect existing Iran-related business interests of European companies and individuals following the US withdrawal from the JCPOA being a clear example.

In respect to the Blocking Regulation, we prepared a July 2018 briefing paper on *'Issues and Considerations for the Finance Sector'* in order to advance dialogue with EU authorities on the practical aspects associated with implementation of the updated Regulation. Within this briefing paper we concluded that while the Blocking Regulation has been in place for over two decades (in relation to US sanctions on Cuba), it has rarely been enforced and to date has not been considered by the financial sector (and indeed other sectors) to offer any real protection against the applicable scope of US sanctions.

Nonetheless, the amended Blocking Regulation has added a further dimension of legal complexity and cross-border compliance challenges. Additionally, the Blocking Regulation has created an unintended consequence whereby EU located financial institutions have, in some instances, come to the opinion that they have little option but to exclude themselves from all Iran related activity, even activity permissible under US sanctions. This is driven partly by European Commission guidance, which indicates that seeking assurances/or a licence from OFAC would be in contravention of the Blocking Regulation. This appears inconsistent with the objectives of promoting permissible activity with Iran, and is also contradictory to the approach that several member states (Italy and Greece) have taken, in applying for oil waivers from the US Department of BIS. Indeed, the UK Government has supported a specific licence from OFAC for the continued operation of an oil field in the North Sea, which has Iranian Government ownership. Our members strongly recommend that communication channels with OFAC need to remain open to facilitate permissible payments.

For Iran and beyond, exceptions and exclusions that support the continuation of permissible business and humanitarian activity have traditionally formed part of all major sanctions regimes. However, in recent years it has become gradually more challenging to distinguish relationships or activities which are unequivocally prohibited from those which are permitted. A salient example of this was the introduction of sectoral sanctions placed on certain Russian, government-owned banks, energy companies and defence

companies following the annexation of Crimea and escalating Russian interventions in Eastern Ukraine. Broadly speaking, these sectoral sanctions restrict access to the loan and capital markets in the US and EU and are less restrictive than blocking/asset freezing sanctions. While the concepts of debt and equity appears relatively simple in the abstract, their application has been highly complex to determine in terms of breadth and complexity of implementation.

Beyond sectoral sanctions, ownership and control factors plus expectations on banks to ascertain 'indirect' sanctions risk exposure (e.g. through correspondent banking network relationships) have further necessitated more intensive risk management responses. Where sanctions are open to broad interpretation, as seen with EU and US Russian sectoral sanctions, and/or lack sufficient implementation guidance, this often results in financial institutions adopting a highly cautious approach. This in turn may result in significant elements of what would otherwise be 'permissible activity' being discontinued due to some element of potential sanctions risk.

The US experience, where the de jure reach of US sanctions is extremely broad, has in practice led to US sanctions often extending well beyond the legal grasp of US authorities. Consequently, with the interdependence of international financial markets and international spread of large companies, US sanctions have a significant chilling effect even on non-US subjects. For instance, UK and indeed EU, banks remain extremely cautious about being exposed to any dealings with Iran, for fear of incurring US fines or being excluded from US financial markets as a result of a secondary sanction being imposed. Dozens of major international banks have "de-risked"— exiting customers and even whole lines of business due, at least in part, to perceived direct or indirect sanctions risks and the potential commercial risks that may arise from a sanctions violation penalty being applied.

The introduction of the impending UK legal sanctions framework will undoubtedly introduce a new and extremely important dynamic within the US-EU sanctions architecture. Globally operating corporate and financial institutions will increase scrutiny of the approach taken by the UK toward pursing unilateral sanctions and extra-territorial enforcement activity. We would not wish either EU or overseas business to withdraw from the UK due to legal uncertainty, nor for this to impede business reacting to potential future relaxation of sanctions, where operational complexities associated with unintended consequences force a more cautious commercial approach.

Broadly speaking our members would support the view that sanctions, when used effectively as a complement to other diplomatic tools, are a preferred initial course of action to encourage a change in behaviour by a sanctions target, not least by sending a message that previous behaviour is not acceptable. UN, US, EU and UK sanctions absolutely have a significant impact in influencing business decisions, which in turn may be deemed to be an effective tool in creating change. But to ensure real and sustained impact, our members note the importance of the following criteria:

- **Multilateralism – At the implementation level the most successful sanctions programmes are those imposed by a number of countries/international bodies at the same time**. As an example, sanctions on Iran prior to the JCPOA were increased by the US, the EU and the UN. Such coordinated action sent a clear message to industry and was high influential in determining global business decisions in respect to Iranian exposure. Arguably less successful are regimes where there is little support from a wider group of countries. In terms of overall financial restrictions imposed, UN sanctions are generally the most limited, although they carry the greatest legitimacy in the international system and often create the legal basis for more forceful financial measures by individual states and the EU. Despite their higher level of perceived legitimacy, timely implementation of UNSC Resolutions within national legislation can vary greatly. Beyond the UN framework, concerted unilateral and regional measures by like-minded countries have by far been the most influential in terms of comprehensiveness, extra-territorial reach and robust enforcement. This has been most obvious in cases of sanctions being imposed against Iran (pre-JCPOA), Syria and Russia where action, in some of these instances, involved co-ordinated measures being pursued jointly by the US, EU and other like-minded countries such as Canada, Japan, Australia and New Zealand. However, our members also note that the legitimacy in how countries such as the US, EU member states and like-minded partners impose sanctions is a complex matter and within the UN, especially the General Assembly, there is no

consensus of opinion on whether the use of unilateral, coercive, economic measures are achieving their desired impact.

- **Political will, clear goals and co-ordinated roll-back provisions – Effective sanctions have a clearly stated objective and end goal.** Recognising that no two sanction regimes are the same is of paramount importance for ensuring appropriate implementation. Our members view understanding the political objectives behind each sanctions programme and their related regulations as an essential first step in managing the associated risks and designing the control environment. Consequently, the financial sector follows closely the fluidity of how and why sanctions are imposed, and indeed what grounds may result in their lifting.

  The legal framework for imposing sanctions will impact on the process for rolling them back. By their nature open ended sanction regimes (i.e., those containing no fixed periodic timescales for formal re-approval) can make continuation much more likely than termination. This is especially the case if the objectives of the sanctions regime lack clarity, cover a broad range of issues within a singular piece of sanctions legislation (i.e., those that merge parallel concerns such as human rights, terrorist concerns and nuclear issues) and are therefore more likely to be open to wider interpretation as to whether the original intended goals have been met. As demonstrated in the case of Iran, easing sanctions can be a lengthy process that is both legally and politically difficult. Our members further note that where sanctions are imposed by the US Congress, the roll-back process can become more difficult and slower to lift. In certain scenarios, e.g. Cuba and Iran, the US executive branch can only go so far to lift or waive sanctions as a complete lifting will require new action by Congress.

  Consequently, where financial institutions seek to navigate the sanctions-lifting environment they often face challenges of disconnect across major sanctions roll-back regimes. Salient examples include Myanmar, Belarus and Iran. In those cases the sanctions easing process has been marked by notable differences between the EU and US regulatory frameworks. Moreover, the on-off nature of certain regimes has further resulted in financial institutions having to view exposure through a much longer-term lens, for example in the cases of Libya and Iran.

  The nature of sanctions relief as part of the international roll-back process can often be characterised as highly complex. This was illustrated most clearly in the case of Iran where commitments by the US on the one hand and other signatories on the offer under the JCPOA varied considerably and created significant compliance challenges for global financial institutions. For instance, US sanctions relief was provided through the issuance of a new Executive Order, new general licences, a new statement of licensing policy, and new Guidance and FAQs, as well as the adoption of several statutory waivers and the delisting of various individuals and entities from the Specially Designated Nationals and Blocked Persons (SDN)/other sanctions lists. These measures lifted nearly all nuclear related secondary sanctions applicable to activities of non-US persons relating to Iran, including restrictions on the Iran-related activities of non-US entities owned or controlled by US persons.

  By contrast, the vast majority of US 'primary' comprehensive sanctions against Iran remained in force even whilst the US remained a party to the JCPOA, as did US secondary sanctions targeting Iran's support for terrorism, human rights abuses, ballistic missile development and destabilising regional activities, remained in effect. EU sanctions programmes targeting human rights abuse and ballistic missile activity in Iran also remained in effect. In addition, at the time of the JCPOA entering force, half of US states had restrictions on companies that do business in Iran with the most frequent being measures to block investments of pension funds and government contracts and most of these programmes were neve rescinded.

The advantages and disadvantages of the EU's approach to the use of sanctions, both generally and in specific cases (such as Russia)

The EU's approach to sanctions has been to impose more focussed sanctions targeting specific parties or sectors compared to the US, which has historically been more inclined to impose very broad country-wide (or comprehensive) embargoes supported by General Licences or certain exemptions. The advantage of the EU approach is to try to narrow the impact of sanctions to the true target of the sanctions and to limit

the impact of such measures on the wider population of a specific country. The disadvantage to this approach is that the more targeted the sanctions, the easier they are to circumvent. For example, despite both US and EU sanctions, the targeted Russian government entities have still been able to raise capital.

When assessing the impact of sanctions, the clarity of the ownership and control structures becomes of paramount importance and can be one of the most complex elements of ensuring sanctions compliance. This is especially true in the case of recent US and EU sanctions targeting Russian entities and individuals. Under EU sanctions, ownership or control is established in accordance with set criteria and making available funds or economic resources to non-listed legal persons or entities owned or controlled by a listed person or entity will in principle be considered a sanctions breach.

The EU, and indeed many other jurisdictions (e.g. the US), tends to apply a 50 per cent rule and criterion to establish the ownership of an entity to ascertain whether it is subject to sanctions restrictions. For example, if a listed individual has 50 per cent or more ownership of a non-listed entity, UK persons/entities are prohibited from making available funds and economic resources to that entity. The concept of 'control' may, depending on the situation, not work to the same 50 per cent threshold. In comparison to the US focus on ownership, the concept of 'control' under EU sanctions is a somewhat looser concept and is open to wider interpretation depending on the sanctions regime and issues at play.

The advantage of the EU concept of 'control' is that it enables restrictive measures to have an impact where individuals/entities own less than 50% of a company but control the company (e.g. the ability to decide membership of the board of directors or a designated person selling their shares to a family member/business partner but where the designated person still has control).

The disadvantage to the EU approach is that it provides less legal certainty and is far more difficult for EU financial institutions to comply with. With the US approach, it is a more straightforward process to know whether to block/freeze property of a company owned by the designated person. With the EU concept of control, there is far greater ambiguity about whether a designated person might control a company (e.g. if a member of the board of directors is designated, it is very hard to know how much influence they might exert on the company and this can lead inconsistency of application) and leads to uncertainty as to the level of due diligence required. We have strongly impressed on the UK Government the need to consult industry on how they may wish to define control in the application of sanctions post Brexit.

Although US specific in context, the 6 April 2018 US sanctions under the US CAATSA regime are illustrative of the challenges of implementing ownership and control obligations – even in instances that do not include the more complex EU approach. The April 2018 CAATSA sanctions, which targeted a handful of Russian businesses and individuals, in effect resulted in thousands of non-listed entities, many of which were located in the EU, also becoming the target of sanctions.

Our members strongly believe that the future UK sanctions regime should seek to ensure a consistent definition of control and ownership that will be applied to all the UK sanctions to minimise the risk of having inconsistent definitions. We understand the Government is seeking to advance this proposal and strongly urge consultation with industry on how ownership and control are defined.

Our members would further highlight that typically securing implementation guidance for a major EU sanctions regime can be a slow and highly ineffective process. Guidance issued at the EU level requires full member state approval, which significantly slows down the ability to issue guidance / Frequently Asked Questions. This was particularly noted in response to the imposition of EU Russia focused sanctions in 2014 where the EU Regulations provoked major aspects of implementation uncertainty.

The subsequent guidance which was issued was both slow and incomplete and resulted in notable member state variation on what activities competent authorities view as permissible or prohibited. A salient example of the EU and US variation in the issuance of guidance was the approach the EU took to certain derivative contracts in 2014. At the time, despite industry calls for further clarity, no EU member state issued guidance on restrictions on derivative contracts. In contrast, the US approach was to issue a General License in September of that year authorising certain transactions involving derivative products whose value was linked to an underlying asset that constitutes the debt or equity issued by a sanctioned party.

In short the US approach can, when necessary, respond rapidly to key implementation uncertainty. The April US CAATSA designations has broadly been seen by our members as a model whereby the US rapidly responded to implementation uncertainty and key wind down challenges. The US issued a range of General Licenses and the Frequently Asked Questions on, among other things, what would need to happen for EN+ to be delisted and whether it was permissible for US persons to purchase Rusal product produced after April 6th (but pursuant to a pre April 6th contract).

How the USA sets and uses sanctions as an instrument of foreign policy, and the advantages and disadvantages of its approach particularly where that differs from the EU

As mentioned above, in contrast to the EU the US often imposes country-wide embargoes then issues General Licences authorising particular activity. These are often accompanied by 'Frequently Asked Questions'. The advantages of this approach is that it provides greater clarity, in that people know a country is off limits unless it is a specific type of transaction that qualifies under a General License. Country wide embargoes also makes circumvention more difficult as it forces transactions to be routed via a different country. However, the challenge with this approach is that it has a disproportionate impact on the wider population of a sanctioned country (though the US may argue that the people help force the government to change approach).

There have been some instances whereby US sanctions have been removed in response to changes in behaviour of the targeted government, particularly Sudan and Burma/Myanmar in recent years. Nonetheless, we also seen the US ever expand certain sanctions programs to cover a wide range of behaviours without a clear indication of how those sanctions could be lifted. For example, the US sanctions on Russia began as a response to the situation in Crimea and Eastern Ukraine and sanctions relief was predicated on the implementation of the Minsk agreement. However, in response to more recent events US sanctions have increased to cover election interference, activity in Syria and Salisbury, but it is not clear which sanctions are tied to which area.

How the UK might best make use of the Magnitsky powers included in the Sanctions and Anti-Money Laundering Act 2018

The introduction of Magnitsky style sanctions are viewed as a further tool that the Government may utilise in response to human rights violations. The effectiveness of such measures will entirely depend on how they are applied. We are willing to work with UK government departments to assist future deliberations on this matter.

In December 2016, Congress passed a new global version of the Magnitsky Act to address human rights abuses on a global scale. We observe that the US approach has been to gradually broadenthe scope of these global measures through executive orders by removing the requirement for 'significant corruption' to just 'corruption'. On whatever basis the UK government decides to proceed there will be an imperative need to define clearly, and offer associated guidance on, what activities are human rights abuses and/or corruption.

The extent to which the UK should seek to align with the EU in sanctions policy post-Brexit, versus areas in which it may wish to diverge or seek stronger sanctions

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.

Our members note indications from the Government that the UK will not seek to diverge from current EU sanctions policy and will continue to coordinate with the EU and other international partners, including the US. We overwhelmingly support this approach but also recognise that differing EU-UK legal structures and political foreign policy priorities will, over time, result in a likely element of UK-EU sanctions divergence.

As currently implemented, the design of EU sanctions requires the consensus of all individual member states and as such ensures a strong degree of coordination in response to common defence and security threats. EU harmonisation 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. 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 sanctions measures is far more influential. This has been particularly notable in cases where achieving UN Security Council consensus has been unsuccessful (e.g. in response to Russia's involvement in Eastern Ukraine and the Syrian conflict) or more limited in nature (e.g. Iranian sanctions prior to the international nuclear agreement).

Post-Brexit divergence between EU and UK sanctions (e.g. where there are 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 we believe would weaken the overall effectiveness of both EU and UK 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 regarding UK nationals working in EU financial institutions) similar to those faced by financial institutions employing US persons.

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

Continuing UK-EU interaction will also provide a strong platform for reducing divergence of approach with other key actors, notably US sanction 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.

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. In June 2018, President Putin signed into law counter-sanctions legislation in response to US sanctions imposed on Russia earlier in the year. The legislation gives the president, among other things, the power to sever ties with 'unfriendly' countries and to ban trade of goods with those countries. If the UK were to adopt a more forceful unilateral sanctions policy separate to the EU this may increase the vulnerability of UK plc, including banks, to retaliatory sanctions by foreign governments.

Moreover, the UK working in collaboration with the EU is well positioned to offer an aligned negotiating position by offering sanctions easing as a support to political negotiations with target countries. This is especially important given that amending or rolling back sanctions regimes to make them more permissive can be legally and politically difficult in the US. As demonstrated in the case of Iran and Cuba, easing sanctions often encounters significant political domestic opposition from those within the House of Representatives and the Senate who may endorse a more hard-line approach. There is no reason to assume sanctions easing in the case of Russia, or other complex regimes such as Syria, will not experience similar challenges. In short, comprehensive sanctions rollback can take many years, or even decades, because of how the US political process operates. We therefore recommend that the UK, working alongside the EU, should ensure they are able to offer a coordinated approach to sanctions easing in order to incentivise a change of behaviour among those subject to sanctions.

The FCO's record in:

- Identifying individuals, companies and regimes that should be sanctioned

The FCO should make a greater effort to designate companies that they know are owned or controlled by a designated person. This would reduce legal uncertainty as to whether certain entities should be subject to sanctions and therefore offer a wider chance for implementation effectiveness.

The FCO should ensure that sufficient identifying information is made available in a designation to allow financial institutions to screen effectively, implement restrictive measures on targets promptly and dismiss false positives quickly.

We further highlight our April 2018 Parliamentary Briefing, issued jointly with Global Witness and Transparency International, on *'Understanding who owns UK businesses: improving the accuracy of beneficial ownership data'.* Within this briefing we emphasised how Companies House does not currently have the role or resources to sufficiently monitor and ensure the integrity of data that is submitted to them for the Register of Persons with Significant Control (the PSC Register). This allows a significant amount of false and misleading data to be submitted, resulting in data quality problems that add significant costs and uncertainty to customer due diligence requirements. Both data validation – to check for completeness and reasonable answers – and data verification – to check the accuracy of all PSC data – are needed to ensure an effective PSC regime. There is also a risk that some of this misleading data is purposefully being submitted to obscure the identity of sanctioned actors and/or individuals using UK companies to launder money.

- Linking specific sanctions recommendations to broader foreign policy goals; and,

Please see our comments below on the need to streamline foreign policy goals with parallel UK commitments to support humanitarian assistance within sanctioned and fragile environments.

- Working with other departments, agencies and the private sector to share intelligence and implement sanctions effectively

Issuance of Guidance

Section 43 of SAML imposes a duty on the appropriate Minister to issue guidance accompanying sanctions regimes. Section 43(2) lists what this guidance 'may' include: best practice for compliance with sanctions, details about enforcement, and details of relevant exceptions. It could be argued that this grants the Government a degree of flexibility, especially in including what type of guidance to issue as it relates to certain circumstances. Similarly, it could be posited that it provides the scope to consider other non-exhaustive types of guidance which would have been unfeasible to address with primary legislation.

Over recent years, our members have extensively worked with the Office of Financial Sanctions Implementation (OFSI) to highlight areas where current UK guidance is outdated, inadequate and at times incorrect. In general, our observation is that the majority of EU competent authorities are often reluctant to issue any detailed guidance to support effective implementation of major sanctions regimes.

The lack of current available guidance may be due to the fact that securing EU-wide 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 (e.g. processing humanitarian aid into Syria) where there is likely to be some type of engagement of a designated party.

In moving forward to a more effective regime we strongly urge that OFSI issue updated guidance that accurately reflects the realities of today's sanctions regimes. We have offered substantive comments to OFSI on the priority areas for update and welcome the focus they are placing on this issue. In addition to our existing contributions to OFSI we wish to highlight the following two aspects where future guidance may be required:

Designations via description: novel powers exist under SAML for a Minister to create new listings by reference to a description. This power is subject to requirements including that a reasonable person would be able to determine whether a specific person would fall within that description, and that it is not

practicable for the government to identify and designate by name all the persons falling within that description at the time. This power has the potential to create divergence between the UK and EU lists of designated entities. This power creates an area for divergence between the UK and EU regimes, and could create uncertainty for institutions tasked with identifying individuals who meet a description, particularly if that description is broad, or requires individual-by-individual research.

Discretion under regulations: regulations made under SAML will make provision as to the meaning of any funds, economic resources or technology being "owned by a person", "held by a person" "controlled by a person" or "made available to the benefit of a person". Additionally, regulations will also make provisions as to the meaning of a person "owning" or "controlling" another person, and being "associated with" another person. These are important areas for sanctions compliance, and one that could vary from regulation to regulation, and across the UK and the EU. Although SAML suggests that the UN and EU approach to "control" is likely to be followed, rather than the US approach of considering majority ownership only, the percentage of ownership and/or indicia of control necessary to extend sanctions remains unknown.

Creating an honest and open public-private dialogue on what is viable and proportionate in the field of sanctions compliance should be viewed as an absolute priority

In this regard, we regularly liaise with UK, EU, US and UN authorities on the need to promote wider public-private dialogue. For instance, we are currently working on a project focused on the future effectiveness of sanctions screening and in particular domestic payment screening provisions. It is imperative that industry and government develop a more open and trusted dialogue on what is and is not possible within the context of sanctions compliance.

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 clearly communicates jurisdictional scope as to how wide the net will be cast. Despite the Government offering some description on the approach to be taken, our members remain concerned that the 'jurisdictional' description will be left rather open ended. Also, it is not clear who will be held ultimately responsible for breaching sanctions where the UK nexus is a step removed (e.g. a GBP denominated financial instrument traded overseas or a GBP transaction between two non-UK entities that eventually clears through a UK financial institution).

We therefore recommend that the Government, or an appropriate regulator, is mandated to issue guidance on what structures of governance and relationships would, and would not, introduce a UK element for sanctions enforcement purposes. We feel this will be important in order to give the business and financial community post-Brexit certainty on their legal exposure and related compliance responsibilities. We have expressed a willingness to work with the Government to support their thinking on developing such guidance.

Reporting obligations

In parallel to defining the UK nexus, we have consistently recommended to the Government the need to set out a clearer articulation of reporting obligations which are placed on industry. This is particularly the case where the situation does not involve frozen assets, or constitutes a clear sanctions breach, is a rejected payment, or where the firms becomes aware another firm may have breached sanctions.

Enhanced information sharing powers

Beyond the current powers provided by EU law, and with the expectation that all of those will be onshored under the European Union (Withdrawal) Act in the event the UK leaves the EU without a new relationship in place, the Government could seek to ensure the introduction of enhanced information sharing powers for sanctions matters 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. We have provided in separate correspondence greater detail on the future requirements for enhanced information sharing powers.

Opportunities to improve implementation effectiveness of licensing

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, improve overall implementation effectiveness and ensure sanctions are appropriately targeted.

Our members are of the opinion that the narrow approach that has typically characterised the licensing regime in the EU has had 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. Our members are clear that the UK's departure from the EU offers a timely 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 wishes to remain competitive within international trade and global finance.

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.

Recognising 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?

SAML offers the ability for the UK to 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).

A further example of where the issuance of a UK General License may be desirable relate to instances whereby a bank may be required – as a result of restructuring, Brexit or for other commercial reasons – to move funds internally for the purposes of preserving an asset freeze.

We welcome the opportunity to progress toward a more effective licensing framework and have offered detailed comments to the Government on this matter. The following section sets out specific proposals in the field of supporting humanitarian payments and which reflect extensive member deliberation over recent years.

Moving toward a forward leaning and proactive approach to UK licensing of humanitarian transactions

Banks and international non-government organisations (INGOs) have increasingly articulated that the current framework permitting humanitarian transactions into sanctioned and conflict environments needs dramatically re-thinking and updating. In short, a new equilibrium needs to be found that recognises the strategic importance of facilitating both humanitarian aid and permissible civilian transactions to higher risk jurisdictions subject to economic sanctions while balancing expectations of appropriate sanctions compliance and counter terrorist controls that are required to make such movement of funds.

Banks and their international charity clients are currently required to navigate a combination of complex multi-jurisdictional regulatory guidance and an inconsistent licensing regime which has led to a significant impact on the funding of humanitarian projects into certain conflict zones and other high-risk countries subject to sanctions. In addition, the broader financial crime risks arising from the Financial Action Task Force citing certain types of non-profit organisation as targets of terrorist financing has led to non-profit

organisations increasingly becoming identified as higher risk clients subject to enhanced due diligence and, in some cases, exit.

Our members have been at the forefront of advancing a range of initiatives with key stakeholders that explore opportunities for creating a more conducive international regulatory and legal environment in support of humanitarian transactions. We believe that as the UK will be required to develop a new approach toward licensing, this will offer a clear opportunity to advance the following proposals aimed at better enabling the processing of humanitarian transactions into sanctioned environments. These include:

- *mutual humanitarian licensing recognition/up front.* Where governments have aligned foreign policy objectives to impose sanctions on a given country consideration should be given to developing an upfront framework that offers a degree of mutual recognition for humanitarian licenses issued by 'like-minded' competent authorities. Such a framework would offer greater confidence to both banks and INGOs. It would further reduce extensive compliance costs and time involved in liaising with multiple individual government authorities. A notification arrangement among licensing authorities could be established to ensure transparency across government stakeholders. A more advanced option would be the utilisation of a pan jurisdictional humanitarian licences arrangement, the benefit of which would be overcoming current multi-jurisdictional and multi-regulator licensing requirements. We appreciate this approach is not straightforward and will require a significant change of mindset among individual competent authorities. Despite this, it should be recognised that without substantive change legitimate humanitarian transactions will continue to experience multiple delays or may need to use less transparent and safe mechanism to move legitimate funds. We would be happy to offer detailed examples to the Committee on the very real challenges currently faced across a range of sanction regimes but in particular in respect to Syria;

- *utilisation of general licenses pertaining to humanitarian permissions.* EU legislation is currently not designed to issue Europe-wide general licenses to cover humanitarian activity. The new UK framework as set out in SAML will enable a greater ability to adopt a general licensing approach that facilities legitimate humanitarian activity. We have stressed our willingness to work with the Government to help shape their thinking on the types of general license most required. In addition, where possible, governments, as part of their donor arrangements, should consider offering conditional approval/appropriate licences at the outset of projects they intend to fund. The UK Government should consider exploring the incorporation of necessary licences 'up-front' as part of the funding agreements for projects operating in countries subject to sanctions. For instance, the Department for International Development as part of their agreement to fund a specific project (e.g. in Syria) could work with OFSI to ensure that the same project receives the necessary UK Government approvals/licences to enable its delivery. Such approvals may include agreements on payment routings and due diligence requirements in advance;

- *pre-authorisation for project activities.* Where an INGO is operating in a highly complex sanctions environment, UK authorities should explore establishing a pre-authorisation framework at the outset of the project. As has been seen in the US context, this may include known engagement with a designated entity, for instance where it is clear that the will require some interaction with a designated entity if it is to operate (e.g. purchasing fuel within Syria so as to operate hospital generators or water drilling equipment);

- *general exemptions for certain mission critical activities.* In rapidly changing conflict situations the window of opportunity to deliver aid is often time critical. Where there are immediate 'life and death' concerns competent authorities should consider the use of an emergency licence or authorisation framework similar to those written into previous EU Regulations which allow for post execution authorisation. For example, military operations to recapture ISIL controlled territory in Syria have resulted in the rapid movement of civilian populations requiring immediate access to food and medical provisions. Such interventions will often be delivered by air drop and are likely to involve engagement with sanctioned entities; and

- *the creation of fast-tracked procurement/licensed channels in major humanitarian emergency situations.* Conflict situations often experience critical shortages of essential medicines, pharmaceutical

products, medical equipment and dual use goods. Given the level of reluctance among western suppliers to offer such goods (in part, for fear of sanctions and divergence issues) the US, EU, UK and UN should work together with INGOs to identify priority needs. These should be shared via a public-private sector platform with relevant suppliers. Such dialogue could not only help to energise the private sector's appetite for supplying necessary humanitarian goods and related financing into conflict and sanctioned environments but also address expected issues in respect to diversion and clarify the necessary licenses available.

The use of sanctions alongside other tools designed to combat dirty money, such as unexplained wealth orders

At this stage we are not able to offer any definitive views on the use of unexplained wealth orders given their relatively recent introduction. However, we do note that the Government will wish to consider a wider tool set beyond formal sanctions when dealing with concerns related to illicit activity, such as money laundering and misappropriation of state assets.

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