

UK's Red Alert on Financial Sanctions Evasion Signals Regulatory Alignment on Future Sanctions Enforcement

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08 / 01 / 22

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Amid the continued rollout of new sanctions measures in response to Russia's invasion of Ukraine, the U.K. National Crime Agency (NCA) and HM Treasury's Office of Financial Sanctions Implementation (OFSI) have jointly issued a [Red Alert](#) (the Alert) intended to promote awareness of the common techniques Russian elites are suspected of using in order to evade financial sanctions.¹

The Alert, published on July 12, 2022, is a product of ongoing collaboration between the National Economic Crime Centre (NECC), a multiagency unit of the NCA designed to coordinate responses to financial crime from law enforcement, regulators, government and private industry, and the Joint Money Laundering Intelligence Taskforce, a collaborative body of banks, law enforcement and regulators managed by the NECC.

The Alert aims to provide information on common techniques which designated persons (DPs) and their enablers² in the U.K. are using to evade financial sanctions. In particular, the Alert warns that DPs are using their associates — including family members and close contacts — via certain enablers to transfer assets to trusted proxies, sell assets at a loss before sanctions take effect or reduce their ownership stakes in investments to below the thresholds which would be caught by financial sanctions.

The Alert is indicative of the heightened approach of U.K. authorities toward sanctions evasion and serves as a warning to professional services firms and corporates of an increased regulatory appetite toward purported enablers of sanctions evasion. This will be of particular importance to businesses, given the recent introduction of the strict liability test for breaches of U.K. sanctions.³ [OFSI Director Giles Thomson](#) stated that the Alert “outlines the significant exposure that many sections of industry have to sanctions evasion, and given the nature of the risks identified, is something we will all need to be increasingly vigilant to.” Thomson's comments echoed those expressed in a recent House of Commons Foreign Affairs Committee report which called on the government to strengthen legislation in order to hold enablers of sanctions evasion to account.⁴

In this article, we set out the key indicators of sanctions evasion and industry recommendations detailed in the Alert, the interplay among U.K. regulators, analogies with money laundering reporting obligations and what the Alert means more broadly for corporates going forward.

¹ This client alert is for informational purposes only and does not constitute legal advice. Complex assessments often have to be made as to which sanctions regime applies in any given instance, given the multinational touch points of many entities and individuals. In that regard, given the complex and dynamic nature of these sanctions regimes, there may be developments not captured in this summary. Moreover, while the summary was accurate when written, it may become inaccurate over time given developments. For all of these reasons, you should consult with a qualified attorney before making any judgments relating to sanctions, as there are potentially severe consequences of failing to adhere fully to sanctions restrictions.

² Enablers are individuals or businesses which may be facilitating sanctions evasion. The Alert notes that key professions in this respect include barristers and solicitors, accountants, investment advisers, estate agents and company directors.

³ By virtue of the Economic Crime (Transparency and Enforcement) Act 2022, OFSI recently obtained new enforcement powers in relation to sanctions breaches. In particular, for breaches of financial sanctions in the civil context that are committed after June 15, 2022, OFSI is able to impose civil monetary penalties on a strict liability basis (*i.e.*, OFSI no longer has to prove that a person had knowledge or reasonable cause to suspect that they were in breach of financial sanctions).

⁴ House of Commons Foreign Affairs Committee, “[The Cost of Complacency: Illicit Finance and the War in Ukraine](#),” Second Report of Session 2022-23 (June 30, 2022). See paragraph 23 of the report: “The vectors of illicit finance are often companies. Therefore, the FCDO should work across Government to encourage reform of outdated and ineffective corporate criminal liability laws which mean that it is difficult to hold large companies to account for economic crimes.”

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Indicators of Sanctions Evasion

The Alert outlines three areas of possible sanctions evasion: (i) **frozen asset transfers**; (ii) **U.K. enablers**; and (iii) **suspicious payments**.

Frozen asset transfers. Indicators include changes to the beneficial ownership of DPs' corporate structures prior to, or shortly after, sanctions taking effect; the use of trust arrangements or complex corporate structures involving offshore companies; ownership transfers to previously unknown individuals; and the use of non-Russian or dual national family members or associates to act as a front, allowing the DP to maintain indirect control.

Enablers. Indicators include the use of banks and financial organisations owned by close associates of DPs, evidence that an enabler's own due diligence relies on a further layer of diligence they do not themselves conduct, and a large volume of off-the-shelf corporations with no trading record and with nominee ownership being used as throughputs.

Suspicious payments. Indicators include holding companies based in jurisdictions that are offshore and/or historically linked to assets in the former Soviet Union, and transactions by holding companies linked to DPs with Swiss bank accounts and legal persons from the British Virgin Islands and Cyprus.

Industry Recommendations

The Alert sets out six industry recommendations:

1. **Documentation of transactions.** Financial institutions and professional services firms are advised to document all arm's length transactions and not take them at face value. If in doubt about the legitimacy of a transaction, firms are encouraged to seek guidance from OFSI.
2. **Robust due diligence.** The Alert notes that a failure to undertake appropriate due diligence, including wilful blindness in relation to the source of funds or wealth checks, will be considered a red flag for complicity and may result in both breach and/or circumvention offences.
3. **Assessment of complex corporate structures.** Firms are encouraged to carefully assess complex corporate structures as part of their enhanced due diligence for high-risk clients and to query the commercial justification for such structures.
4. **Caution in relation to aggregation of ownership.** Firms are advised to seek guidance from OFSI if they have any doubt as to issues of aggregation of ownership.
5. **Consultation with competent authorities in relation to changes in ownership.** When presented with documentation that purports to present a change in ownership by a company linked to a DP, firms are encouraged to both conduct enhanced due diligence and consult the relevant competent authority (OFSI in the U.K.) to understand if there is reason to believe that ownership has not been transferred appropriately.
6. **Independent legal assessment in relation to changes in ownership.** Where companies have provided their own legal assessments regarding a transfer of ownership, firms are encouraged to carry out their own legal assessments in order to come to their own determination.

Interplay Among Regulators

The Alert is indicative of ongoing collaboration among multiple regulators and government task forces, and illustrates that the U.K.'s sanctions framework itself falls within the remit of a broad range of regulatory authorities. For example, the Alert includes references to guidance issued, or action taken, in relation to sanctions compliance by the Financial Conduct Authority (FCA) and HM Revenue and Customs (HMRC).

The FCA has been particularly active in issuing industry guidance in relation to the U.K.'s sanctions landscape, with a particular focus on the use of cryptoassets to evade sanctions. In March 2022, the FCA issued a [joint statement alongside OFSI and the Bank of England](#) in which it made clear that financial services firms operating in the cryptoassets sector must ensure they are in compliance with the U.K.'s sanctions regime. In particular, the statement outlined a number of sanctions-specific compliance measures which cryptoasset firms were encouraged to consider, such as ensuring robust sanctions screening of customers and their transactions, and ensuring that due diligence processes are sufficient to identify customers who make use of corporate vehicles to obscure ownership or source of funds.

The statement also identified a number of red flag indicators which may suggest an increased risk of sanctions evasion, such as the use of tools designed to obfuscate a customer's location or the source of cryptoassets, and evidence of transactions to or from a wallet address associated with a sanctioned entity. The FCA also recently provided a response to a request for information from the House of Commons Treasury Committee in which it clearly set out its role in sanctions compliance.⁵

⁵ Re: Treasury Committee's Inquiry on Russia: Effective Economic Sanctions (July 4, 2022).

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The Alert reiterates the FCA's focus on promoting awareness of the financial crime risks, noting that it has been working in conjunction with the NCA and NECC to tackle the increasingly widespread practice of money laundering through cryptoassets by professional money launderers, in particular those from Russia.

HMRC also has a role in the U.K.'s sanctions landscape and is responsible for enforcement of the U.K.'s trade sanctions. The House of Commons Treasury Committee made a request for information to HMRC in order to understand its role in trade sanctions enforcement and compliance but has yet to receive a response. The Alert points to HMRC's role in sanctions compliance, noting that HMRC has sent a number of emails to its supervised businesses in relation to navigating the U.K.'s sanctions framework, including certain considerations for businesses to make when transacting with Russia.

Interplay With Money Laundering

The Alert also emphasises the interplay between sanctions breaches and other financial crimes, particularly money laundering offences. Given that sanctions breaches and circumvention of the U.K. sanctions framework are criminal offences, any resultant transfers of funds or assets are likely to become proceeds of crime and therefore be recoverable property under the Proceeds of Crime Act 2002 (POCA).

Suspicious Activity Reports (SARs) have a role to play in sanctions compliance and detecting possible instances of sanctions evasion. SARs are most commonly used to alert law enforcement to known or suspected instances of money laundering or terrorist financing, and are typically made by financial institutions and other professionals such as solicitors, accountants and estate agents. Under POCA and the Terrorism Act 2000,⁶ those operating in the regulated sector⁷ are required to make a report where they know or suspect, or have reasonable grounds for knowing or suspecting, that another person is engaged in money laundering or terrorist financing. Given the Alert's focus on the potential risk of professional services firms acting as enablers of sanctions evasion and its clear indication of a growing enforcement appetite toward such enablers, SARs are an important tool for those operating in the legal, financial services and real estate industries.

The Alert not only reminds businesses operating in the regulated sector of their obligations to make reports to the NCA if they suspect money laundering or terrorist financing activity but goes further, stating that it "welcomes any information identified as a

⁶ Sections 330 and 331, POCA; Section 21A, Terrorism Act.

⁷ See Schedule 9, Part 1, POCA and Schedule 3A, Part 1, Terrorism Act. At a high level, businesses in the regulated sector include those providing investment services, insurance products, company formation services, estate agency work, cryptoasset exchanges and accountancy services.

result of this alert which does not constitute a SAR." In practice, this statement may create confusion by conflating the SAR reporting regime with voluntary reporting. In 2020, it was reported that 573,085 SARs were submitted to the NCA. Against this backdrop, there is a risk that the indicators of sanctions evasion and industry recommendations outlined in the Alert may further contribute to a culture of overreporting and/or overcompliance which regulatory authorities and law enforcement may struggle to contend with.

The United Nations recently published a [guidance note on the dangers of overcompliance](#) with financial sanctions and the detrimental impact on human rights which often follows. The note acknowledged that it is commonplace for financial institutions and service providers to overcomply with sanctions regimes in order to reduce their legal, regulatory and reputational risks, but explained that this overcompliance often contributes to delays and increased costs of delivery of essential goods and services, particularly where charities are unable to transfer funds in order to pay their employees.

Takeaways

The Alert unequivocally signals an increased interest from U.K. regulators in so-called enablers who may be facilitating sanctions evasion and also demonstrates alignment among the various regulators with respect to sanctions enforcement. Although the Alert is nonbinding guidance only, regulators will likely use it when considering enforcement. In particular, the Alert emphasises complex corporate structures as an indicator of sanctions evasion despite the possibility of legitimate reasons why companies and/or high-net-worth individuals may adopt such arrangements. It also cautions that corporate ownership changes made "shortly before" a sanctions designation may be an indicator of potential sanctions evasion, despite the fact that such ownership changes would not be prosecutable if made prior to designation.

With a new strict liability test now in force allowing OFSI to impose civil monetary penalties for sanctions breaches, it is important that businesses, particularly those operating in the legal, financial services and real estate sectors, remain vigilant to the risks of sanctions evasion and associated financial crime risks and ensure they have appropriate due diligence processes in place.

At the same time, it is possible that the indicators and industry recommendations outlined in the Alert will engender an overactive approach to reporting, with businesses keen to limit their exposure to legal and regulatory risks by adopting a risk-averse attitude to reporting any financial crime concerns. The Alert emphasises that firms ought to seek guidance from OFSI when in doubt about particular transactions, but as noted in our [July 11, 2022, client alert](#), OFSI has faced resourcing challenges, also demonstrated by its recent lengthening of response time to licence applications.

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The challenge for corporates will be in navigating compliance with these extensive indicators and industry recommendations while still operating effectively. Corporates will need to take a balanced approach when considering the indicators, industry recommendations and due diligence proposals set out in the Alert as part of their sanctions procedures.

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For additional sanctions updates, see our July 29, 2022, Financial Institutions Regulation and Enforcement alert "[US Adopts Further Sanctions and Export Controls Targeting Russia](#)" and our August 1, 2022, Government Enforcement alert "[EU and UK Adopt Further Sanctions and Export Controls Targeting Russia](#)."