

OFSI Russian Sanctions Penalty; Foreshadows Increasing UK Enforcement?

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On March 31, 2020, the United Kingdom's Office of Financial Sanctions Implementation (OFSI) levied its largest monetary penalty to date of GBP 20.47 million. OFSI penalized Standard Chartered for loans to Denizbank, a Turkish bank that was majority owned by Sberbank, a state-owned Russian bank. Accordingly, those loans violated European Union restrictions on making certain new loans or credit available to sanctioned Russian financial institutions. This enforcement activity may indicate that the United Kingdom regulator is prepared to ramp up its scrutiny of sanctions compliance and to impose increasingly severe penalties in response to violations.

Brief History and Purpose of the OFSI

[The OFSI](#), part of Her Majesty's Treasury, is responsible for maintaining the integrity of, and confidence in, the United Kingdom financial services sector. An important part of that mandate is ensuring that economic sanctions are properly understood, implemented, and enforced, within the United Kingdom. [When the OFSI was established on March 31, 2016](#), then-Chancellor of the Exchequer, George Osborne, announced that the OFSI would be "a centre of excellence for financial sanctions." Financial sanctions, he remarked, "are a hugely important foreign policy and national security tool. Their effective implementation and enforcement are vital to their success."

[Beginning April 1, 2017](#), the OFSI was empowered by the [Policing and Crime Act 2017](#) to impose penalties of half the value of the violative transaction or GBP 1 million, *whichever is greater*. Then-Economic Secretary to Treasury, Simon Kirby MP, explained that "sanctions are a valuable tool against individuals, countries and terrorist groups who threaten UK foreign policy and financial services as well as our national security." Zeroing in on intent, Mr. Kirby added that the OFSI would "take tough action against those who deliberately flout the law." OFSI's Director, Rena Lalgie, insisted the authority would "issue penalties for serious breaches."

The EU's Capital Market Restrictions against Russia and the Trade Finance Exemption

In response to the Crimean Peninsula territorial dispute in the spring of 2014, members of the then-G8 [suspended Russia from the group](#) and the United Nations General Assembly [adopted a resolution](#) affirming the “territorial integrity of Ukraine within its internationally recognized borders.” Further, the European Union, including the United Kingdom, imposed so-called “sectoral sanctions” against a limited number of Russian companies in the banking, oil, and defense sectors.

Those sanctions are contained in Article 5(3) of [European Union Council Regulation No. 833/2014](#), dated July 31, 2014, and Regulation 3(B) of the United Kingdom’s implementing legislation, [the Ukraine \(European Union Financial Sanctions\) \(No.3\) Regulations 2014](#). These sectoral sanctions prohibit any EU person from making loans or credit, or being part of an arrangement to make loans or credit, available to sanctioned entities, where those loans or credit have a maturity of more than 90 days. In September 2014, the restrictions were expanded, including by reducing the maturity date threshold to 30 days. The purpose was to prevent certain Russian banks, companies, and their subsidiaries from accessing EU primary and secondary capital markets.

These restrictions included a carve-out for loans or credit with a specific and documented objective of financing the import/export of goods between the EU and third countries, provided the relevant goods are not restricted by other measures. This “trade finance” exemption, which includes trade with Russia, was designed to facilitate ongoing legitimate trade by the EU member states, but requires that the financed trades concern goods coming in or out of the EU (an “EU nexus”).

Non-Exempt Turkish Loans

[The OFSI assessed](#) that, between April 2015 and January 2018, Standard Chartered had made 70 loans to Denizbank that did not have an EU nexus and thus did not qualify for the trade finance exemption. OFSI estimated their value to exceed GBP 266 million.

However, since the OFSI was empowered to impose civil fines only as of April 1, 2017, it determined the universe of violative transactions to be 21 loans worth GBP 97.4 million. The OFSI assessed combined penalties of approximately GBP 31.5 million, after applying the maximum permissible discount in a case deemed “most serious” of 30%, based on the bank’s self-disclosure and subsequent cooperation. In “serious” cases, a larger discount of up to 50% is permissible.

Standard Chartered invoked its right of ministerial review under [Section 147\(3\)](#) of the Policing and Crime Act 2017. Current Economic Secretary to Treasury, John Glen MP, conducted the review and upheld OFSI’s finding that the loans violated sectoral sanctions and constituted a “most serious” breach of law. However, echoing his predecessor who also had spoken publicly about intent, Mr. Glen found that the bank did not willfully violate the sanctions, had acted in good faith, and had intended to comply with the relevant restrictions. Additionally, Standard Chartered had volunteered the conduct, had cooperated with the OFSI, and had implemented remedial measures. Ultimately, Mr. Glen reduced the penalty assessment to GBP 20.47 million.

Additional Considerations

Although the size of the penalty was a significant departure from past OFSI enforcement, it is clear that Standard Chartered benefitted both by submitting a voluntary disclosure (less 30%) and by appealing OFSI’s penalty via ministerial review (less an additional GBP 11.03 million)

While the resolution of this action hinged on the absence of an EU nexus, compliance with EU

sectoral sanctions is complicated by the absence of any official government lists identifying entities owned or controlled by sectorally sanctioned Russian parties. Therefore, banks and businesses must ensure that they are conducting sufficient due diligence of their customers and counterparties to identify any sectoral sanctions concerns.

Similarly, financial institutions must avoid adopting a generalized approach to reliance on exemptions to sectoral sanctions. Instead, compliance programs must be calibrated to require an EU nexus for every individual transaction that seeks to fit within the trade finance exception. Uncertainty must be escalated to an appropriate authority, to avoid violations. The OFSI at first instance and the Economic Secretary on appeal may have assessed this case as “most serious” since the European Commission had published guidance on the Article 5(3) trade finance exemption in both [2015](#) and [2017](#). Among other things, the guidance emphasizes at Q&A 6 the need for “a meaningful nexus with the European Union, in order for this exemption to apply.”

This is the first civil or criminal OFSI enforcement action related to the EU’s capital market restrictions against Russia. Moreover, this is only the fourth civil penalty imposed by OFSI and by far the largest to date. The second largest, [assessed in September 2019](#), was for just GBP 146,341. In sum, action of this scope and magnitude is unprecedented and potentially could mark the dawn of a new era of sanctions enforcement by the United Kingdom.

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