

Overview

The Financial Conduct Authority (FCA) fined a UK Challenger Bank (Bank) £29 million (after a 30% discount¹ due to failings with its financial sanctions and anti-money laundering (AML) systems and controls. The FCA commented that the Bank had undergone “exponential growth” but that “its financial crime controls [had] failed to keep pace with its growth”.

This is the largest penalty the FCA has issued in relation to sanctions controls and is indicative of the FCA’s continued focus on the financial crime compliance of regulated firms. The Office of Financial Sanctions (OFSI), responsible for enforcing UK sanctions, has also issued several fines for breaches of the UK’s sanctions regulations, with the biggest fine imposed to date being £20.5 million in 2020.

The UK government is extremely focused on sanctions compliance, having recently significantly increased funding for OFSI and having launched a new Office of Trade Sanctions Implementation (OTSI) within the Department of Business and Trade earlier this month. Accordingly, we recommend that firms regularly review their assessments of sanctions risk and ensure that their sanctions compliance frameworks are fit for purpose to avoid risks of sanctions breaches, financial penalties, and reputational damage.

The FCA’s recent findings provide useful insights into expectations around sanctions compliance for businesses in all sectors, but is particularly instructive for disruptive companies that are leveraging innovative financial technology to grow as fast as possible.

Background

The FCA has placed increasing importance on strong financial crime controls in recent years, imposing significant fines for control failures. The FCA’s regulatory oversight of sanctions differs from OFSI and enables it to take enforcement action for systems and controls failings, even where no actual breach has occurred. While the FCA’s regulatory remit is limited to regulated financial services providers, its findings provide helpful guidance for businesses across all sectors when considering the best approach to sanctions compliance.

Between 2022 and 2023, OFSI recorded 473 suspected breaches of financial sanctions (a threefold increase on the previous year) and, as of April 2023, its enforcement unit had 172 cases under live investigation.

OFSI has a range of enforcement tools at its disposal and introduced strict civil liability for breaches of financial sanctions in June 2022. With firms facing significant financial exposure and reputational damage for sanctions breaches, this is an area where proactive focus on prevention is critical.

Overview of the FCA’s Enforcement Action

In this case, the FCA’s enforcement action was foreshadowed by the 2020 National Risk Assessment (NRA) of money laundering and terrorist financing, which set out the key money laundering and terror financing risks for the UK. That NRA identified challenger banks as vulnerable to money laundering, including because of their fast onboarding processes.

Accordingly, in 2021, the FCA conducted a review of the financial crime controls of six challenger banks, including the Bank, across the following areas:

- Governance and management information
- Policies and procedures
- Risk assessments
- Identification of high risk/sanctioned individuals or entities
- Due diligence and ongoing monitoring
- Communication, training and awareness

Following its review, the FCA published examples of good and poor practice. The FCA highlighted the need for financial crime control resources, processes and technology to be commensurate with a firm’s size. It emphasised that a risk-based approach should be applied and that firms should continually monitor their policies and procedures to ensure that they remained fit for purpose. The FCA noted that enhanced due diligence should be applied in higher risk circumstances, with the process formally documented. The FCA also drew attention to the need to adequately manage transaction monitoring alerts and their assessment.

In the present case, the FCA noted that the Bank’s financial crime controls and framework did not grow commensurately to the number of customers it had onboarded, which increased from approximately 43,000 in 2017 to 3.6 million in 2023.

Between 2020 and 2023, the Bank was engaging with the FCA to improve its financial control framework in relation to various concerns that had been identified by the FCA.

1 The Bank would have been fined £41 million, but it agreed to resolve these matters and so qualified for a 30% discount under the FCA’s processes.

Then, in January 2023, the Bank identified a deficiency with its automated screening system, which had only been screening the name of customers against a portion of the names on the UK Consolidated List, which lists all persons designated under UK sanctions. The Bank acted immediately to remediate this issue, however, a wider review of its sanctions framework found multiple other issues. The Bank reported the issues to the FCA and undertook significant remediation.

The FCA findings highlight the following key areas of deficiency:

- There was a lack of understanding of sanctions risk and compliance at senior management level.
- The risk assessment was insufficient to inform risk decisions and management of sanctions-risk.
- The sanctions policies and procedures were inadequate and needed updating and enhancing, including in relation to reporting, testing and management information requirements.
- Roles and responsibilities were not adequately defined.
- The Bank did not test the effectiveness of the configuration of its customer screening or payments screening at or after implementation and so had no way of knowing if the screening programmes were operating effectively.
- No financial sanctions screening alerts were generated over a six-month period, due to a system misconfiguration that affected matching between customers and the sanctions lists.
- The misconfiguration meant that customers were only screened against persons on the UK Consolidated List (and not other countries' sanctions lists) with UK citizenship or residency, in breach of the Bank's sanctions policy. This issue had been present, but undetected, since 2017.
- There was no standalone procedure for sanctions screening alerts, and the general procedure provided no explanation about what an alert was or how to manage alerts.
- There was no management information relating to sanctions alert volumes or trends that would have helped the Bank to monitor the effectiveness of the configuration of its screening programmes.
- There was no assurance or audit review of the sanctions screening programme.
- Screening was not carried out with sufficient regularity (every 14 days where best practice would be daily).
- There was a failure to screen cross-border transactions against the UK Consolidated List.

What Steps Should You Take To Ensure You Are Complying With Sanctions?

To ensure that you are complying with sanctions, we recommend:

- Making sure that you know what sanctions regimes you and your staff are subject to. Consider where you have business operations, customers and suppliers; the nature of your product or service; and how you make/receive payments. Remember to consider the nationalities of your employees and officers.
- Conducting a sanctions risk assessment across your business (i.e. enterprise-wide) if you do not already have one.
- Implementing a sanctions policy if you do not already have one.
- Ensuring that you have appropriate procedures to verify the identity of persons you transact with as part of your business.
- Carrying out screening before onboarding new customers.
- Checking your understanding of your processes – particularly any automated screening – and testing their efficacy.
- Communicating with your staff about sanctions, ensuring that they understand their roles and responsibilities; how to identify and mitigate risk; and that they are familiar with the company's sanctions policy.
- Providing role-specific training where appropriate.
- Demonstrating good governance and oversight of sanctions risk and compliance, with effective management information.
- Reviewing your sanctions framework regularly, including when you have new product lines or services; enter new markets; experience significant growth; and in response to changes in geopolitical situations.



How Can We Help?

Our global Government Investigations & White Collar team regularly advises individuals and corporates on compliance and investigations related to financial crime, including sanctions and money laundering. We help clients assess risks, implement compliance frameworks, and investigate issues when necessary. We have assisted global banks and other businesses with investigations and transactional audits of potential violations of US, UK and other laws, and dealt with related proceedings before enforcement agencies and regulators, including the US Treasury Department's Office of Foreign Assets Control (OFAC), OFSI, the Department of Justice, the New York State Department of Financial Services, and the Central Bank of the UAE.

Recent successes include a no-action letter from OFAC; a favorable settlement with the US Department of State, allowing our client to continue contracting with US government agencies; a no-further-action letter from the National Crime Agency following an investigation into money laundering offences; and a no-further-action letter from the Public Prosecution Service of Portugal following a successful defence involving mutual legal assistance treaty requests made to Swiss banks in relation to alleged money laundering issues.

If we can assist you with these or other matters, please contact us.

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