



HOUSE OF LORDS

# Select Committee on the European Union

## External Affairs Sub-Committee

### Corrected oral evidence Brexit: sanctions policy

Thursday 12 October 2017

10.05 am

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Members present: Baroness Verma (The Chairman); Baroness Armstrong of Hill Top; Lord Dubs; Lord Horam; Baroness Manzoor; Earl of Oxford and Asquith; Lord Risby; Lord Stirrup; Baroness Suttie; Lord Triesman.

Evidence Session No. 4

Heard in Public

Questions 39 - 52

### Witness

I: Mr Roger Matthews, Senior Director, Dechert LLP.

## Examination of witness

Roger Matthews.

Q39 **The Chairman:** Good morning, Mr Matthews. Thank you very much for coming here to give evidence to us this morning. I just remind you and colleagues that this is a public evidence session, and a transcript will be sent to you afterwards. If you would like to make any corrections to the transcript, please make them and send it back to us. We do not normally have opening statements, but it would be useful for the Committee to have a little background from you on your work at the Commission and your current work.

**Roger Matthews:** Certainly. Good morning, and thank you for inviting me to speak today. It would be good to set out a little background. I can see from the questions that a particular area of interest for you is my previous experience at the European Commission, so let me just run through where I am and what I have done in relation to sanctions in the past.

I am now in the international trade and EU law team at Dechert, where I frequently—it is not the sole focus of my practice, but it is a large part of my practice—advise businesses on sanctions compliance and issues relating to sanctions. I have been here for about three years. We have clients across a very wide range of sectors.

Prior to that, I had two other jobs relevant to sanctions, one of which might be of particular interest to this Committee. For three years I was a seconded national expert to the European Commission. In practice, although I was a UK civil servant at the time, I was to all intents and purposes a European Commission official for those three years.

That period was from 2009 to 2012, so when I speak about my experience at the European Commission it is important to understand that it runs up to five years ago. I am aware from my current work how things have evolved since then, but in terms of first-hand experience of how the Commission operates it is important to be aware of that. That said, I do not think that the key fundamental structure has changed massively in that time, but some of the practice has.

The other plank of sanctions experience, which I mention more by way of history, because you have heard from people who have done this more recently, is that for 18 months prior to my secondment to the European Commission, I was in what was then called the Asset Freezing Unit at HM Treasury, which is one of the precursors to what is now the Office of Financial Sanctions Implementation.

Over time, I have seen sanctions from the UK licensing perspective—I was a legal adviser to the Asset Freezing Unit—and then from the policy perspective at the European Commission. More recently, I have been advising clients on sanctions from the private sector perspective.

**The Chairman:** That is very helpful, and I am sure the Committee

appreciates the very quick background information that you have just given us. I forgot to say earlier that you were given a list of questions beforehand. However, I cannot promise that colleagues will always stick to the questions that you have had the privilege of seeing before. If I may start off with a question you would have seen, what role does the European Commission play in the process of designing and agreeing EU sanctions? What was your role in that process?

**Roger Matthews:** It is useful to start by flagging that the European External Action Service was set up in 2010, and so the arrangements between the Commission, the Council and the External Action Service have been something of an evolving beast since then. I actually started at the European Commission in 2009, so I will not bore you with how things worked before the establishment of the EEAS. The account I will give you is how things worked by the end of my time there and, I understand, broadly still do now, save for a couple of evolutions that I will pick up on along the way.

You have heard evidence from government representatives about the more political 'head of steam' that builds up when there is a political desire for a sanctions regime to be put in place or extended. At the political end, that is reflected in the adoption of a Common Foreign and Security Policy decision. That decision is drafted by the External Action Service; it is adopted by the Council. In formal terms, the Commission does not have a particular role in that, although I will come on to the informal side in a moment. The formal Commission role comes in reaction to that CFSP Decision.

The CFSP Decision will essentially set out all the individual sanctions measures that the Council has decided it would like to adopt in relation to a particular country or a particular situation. Those measures could be categorised into two parts. Some of the measures will be Member State competence, i.e. not EU competence. For those measures, the EU has no further role; it is for Member States individually to see that those measures have been agreed by the Council in the CFSP Decision, and to give effect to them nationally. Examples of those would be arms embargoes and travel bans.

The other category is measures that fall within EU competence, such as the trade measures and the financial restrictions. Those are given effect not by Member States individually but by an EU Regulation. That is where the Commission's formal role comes in. The Commission's role is to prepare that Regulation, to draft it, to present it to the Council and then participate in the Council discussion about that Regulation leading to a final product.

Informally, it is fair to say that two things adjust that process. First, it became apparent over time—it was a particular problem with a couple of significant Regulations when I was there—that if that process were followed literally, the External Action Service would propose a CFSP Decision, that decision would be agreed by the Council, and if the Commission only at that stage went away and started its drafting,

particularly on the more complex ones, there could be quite a significant time lag between the adoption of the CFSP Decision, which would be public, and the adoption of the corresponding Regulation.

That can allow for all sorts of problems. It can allow for asset flight, because people who are going to be designated on a sanctions list can see that there is a decision to put them on the list before they are, in legal terms, subject to it. It can also lead to confusion for businesses, because, again, they can see the EU has decided on rules, which are often expressed in some detail even in the CFSP Decision, but they are not yet subject to them, or, very commonly, they do not really know whether they are yet subject to them.

The practice therefore evolved that the Council would like to be in a position to adopt the CFSP Decision and the Regulation together, even though in formal EU Treaty terms there is a sequencing, namely that the CFSP decision should come first. In practice, this has led to the External Action Service, which drafts the CFSP Decision, and the Commission, which drafts the Regulation, working very closely together, essentially to prepare the two in tandem.

Over time, the practice has developed for CFSP decisions to contain more and more detail. Very commonly, the asset freeze measure in the Decision and the asset freeze measure in the Regulation are very close to identical. The more detail that is in the Decision, the more important it is that the Decision and Regulation are drafted together and that the Commission and the External Action Service staff are involved in both.

The other thing that has evolved—particularly, I understand, since I left—is that, with some of the more complex Regulations, there has been an awareness that informally there is a value in having the Commission involved earlier in the process. Even though you might say that in a formal sense there is the first step of a political decision to have sanctions and to broadly identify the measures, and then a second separate step of operationally drilling down on the detail, in practice it is a bit more fluid than that. If you consider the operational detail and the impact on businesses only when the Commission's role comes into play—it steps in relatively near the end of the process—it does not work very well. Therefore, on the more complex Regulations, there has been an increasing awareness of the value of having the Commission involved earlier. Although it was after my time, I gather that was particularly true in the Russia sanctions, for example, where the Commission was very actively involved at a very early stage.

**The Chairman:** Thank you. That was very comprehensive and very detailed.

**Q40 Lord Stirrup:** Could I take you a little deeper on that, Mr Matthews? One of the things we are very interested in is the degree to which sanctions policy and the detail of the policy is, if not decided, then at least given a very fair wind by the detailed donkey work within the engine room, rather than by big cheeses sitting around a table at the end of the process.

Understanding the mechanics of how that happens is extremely important.

You have already talked about the co-ordination with the EU External Action Service. To what degree is that co-operation, and perhaps the co-operation with the Council and other EU institutions, important in this initial process of framing the sanctions? To what degree, in your experience, are the policy decisions and the details of the policy implementation pretty much decided before you get to the decision-making stage?

**Roger Matthews:** Again, that has evolved. Some years ago, there used to be a bit of a problem with co-ordinating the policy decision-making and the mechanics. Often, key decisions, including sometimes quite detailed decisions about how a sanctions regime would be structured, were taken before the people who were best placed to understand at least the impact of those details on business were involved. That was a bit of a problem, but over time that has been recognised as a problem. That is why, even though there has been no change to the formal process, the Commission has, informally, become more involved earlier.

There are a few other things to say on that. One is about how the Commission goes about its decision-making process internally. I was in what was called the Service for Foreign Policy Instruments. That was the residual bit of what used to be DG Relex, which remained with the Commission when the rest of the Commission's external affairs function was shifted to the External Action Service. The Service for Foreign Policy Instruments—which is abbreviated to FPI, if you see that acronym around—holds the pen and leads the co-ordination and control for the Commission at the working level for the preparation of sanctions measures.

Internally within the Commission, though, it involves a number of other Directorates-General and Services. It does that both formally and informally, particularly where you get a long lead-up. Where it is obvious that the political consideration is going on a long time before the formal need to draft, that gives quite a long time to start those consultations with other DGs about what elements there might be and how they might be framed.

Formally, the engagement with other DGs comes together in what is called an Inter-Service Consultation; FPI will prepare the first draft of a Regulation and then run it through this inter-service consultation. Other interested DGs will get to look at the draft and provide their comments. Sometimes DGs that are only tangentially consulted do not have much input, but often the legal service has very extensive input and DGs that have the most active involvement, covering the areas that are most actively impacted, which are commonly energy, financial services, internal market, et cetera, bring quite a lot to the table in those discussions. That might lead to a bit of toing and froing internally within the Commission, which is part of the process by which the draft comes

together. That happens in tandem with the discussions with the External Action Service.

Separately, Member States may at any point in the discussions, when they anticipate particular elements that need to be there or that might be problematic, either for them politically or for businesses in their area, bring that to the Commission and work through with it how the element might be accommodated in the framing of the discussion or later in the operational detail.

One thing that Member States want to know quite early on is whether any implementation issues are something that they need to be alert to politically at the early framing stage or something that the Commission can incorporate and adjust into the drafting when it puts the actual text together. There is no one size fits all. The honest answer is that it depends a little on the circumstances: first, how complex or simple the proposed measures are, which will depend on the situation; and, secondly, how much notice there is and therefore how much time there is to have all the bits of the evolution running together.

**Q41** **Baroness Armstrong of Hill Top:** Most of my question has already been answered. I just want to follow up, because my question was about the formal and informal co-ordination of designing and updating sanctions regimes. As you say, of course Member States will have interests that relate to their own economy and their own interests in any sanctions regime. How would Member States be represented within the staffing and co-ordination role that you are talking about? You explained your role as being from the British civil service within the Commission. Would you say a bit more about that?

**Roger Matthews:** There are quite a lot of players involved in the process. There is a distinction between officials of the Commission, who obviously come from EU Member States but are duty-bound to leave aside their national loyalties and wear a Commission hat, as it were, and the representatives of all the Permanent Representations, who are in Brussels routinely having informal engagements throughout the process and who overtly represent their Member State's interests.

Seconded National Experts are in a slightly unusual position. It is of course expected that, as an SNE, you will have a certain awareness of the interests of your member state, which is why, or is at least part of the reason why, Member States have an interest in sending them. It is nonetheless made clear—and there is sometimes a bit of attention on this—to seconded national experts that formally they are to operate as Commission officials like any fonctionnaire<sup>1</sup>. Now there is a bit of give and take. There was an understanding that I had a much closer relationship with officials in parts of the UK Government than I did with a lot of other Member States, because that was where I had come from, but formally I was as much a Commission representative as anyone else.

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<sup>1</sup> Permanent Commission official

Member States' interests can be represented in a number of ways. If you have a seconded national expert, that certainly helps ease the channels of communication, but it is not the only way. Mine was a team of four people, so there was by no means a suggestion that all Member States had an easy line in to FPI. There were some changes in that the staffing of FPI, but it was never the case that all Member States were represented.

Importantly in relation to informal communications, the formal discussions at Council are done through a working group called the Relex working group, which meets very often. In my day, it used to meet on average twice a week. I suspect it continues to meet with that level of frequency. That means that the individuals—the Member State representatives, the Commission and the External Action Service people who work on sanctions—meet quite often at a personal level. That helps with the informal discussions, which at working level is very important because that is the way the EU identifies whether problems can be solved or whether there are things that need to be escalated to a higher — more senior — level. In the round, that brings all the interests together. Sometimes there are also bilateral opportunities along the side between individual Member States, the External Action Service and the Commission.

**Baroness Armstrong of Hill Top:** Would the critical meetings be frequent and with different groupings?

**Roger Matthews:** As part of the process for deciding the sanctions, the relevant geographical group would take the decision that there should be sanctions in relation to a situation. I was not involved in those geographical groups, which are chaired by the External Action Service, with representatives from all Member States. That is where the political decision would be taken that there should be sanctions. Where there is a list of designated targets, the geographical working groups also have to approve whether there are sufficient grounds for each of those targets.

The framing of the CFSP Decision and the Regulation happens on the back of drafts from the EEAS and the Commission respectively, and it happens within the Relex group that meets twice a week. There is no rigid timetable for the progress of these discussions, although there may be at least an informal one now. There was certainly an expectation that, barring very complex cases, there would be a maximum turnaround. I seem to remember it was two weeks, but very commonly political urgency meant that two weeks was not really possible.

There was no fixed timetable. Essentially, there was a pressure to move these things forward as fast as possible. Even though, as I said, the Relex group met twice a week, that was not rigid. If there was a need for them to meet more frequently in order to get something up the chain of committees in time for a political deadline, that would happen. It is important to understand that, even once the Relex group had reached agreement, that was simply the first stage. If everything was agreed there, it could obviously go up through the chain of committees to the

Council very quickly, but if there were aspects that could not be agreed at working group level, there might be a further round of significant discussion at the next level up<sup>2</sup>.

**Q42 Lord Risby:** I think we can agree that, if sanctions are to be efficacious, the more countries that are involved in this the better. Very often there are synergies between the European Union and other countries in taking the same approach. One thinks of Australia or Canada. Of course, the country that is of most interest, where there is often overlap, is the United States. It would be interesting for the Committee to know, in terms of trying to achieve a common objective, what the interface in methodology is between the European Union and a country such as the United States. We are getting, of course, an example in Ukraine, and potentially more so in Iran. All this is very important for any EU-wide sanctions to have an impact.

**Roger Matthews:** There is certainly an awareness of the value of synergy. You could look at the interface in two parts. One is the interface on specific sanctions regimes and whether there is an interest in aligning and how you align the sanctions on Russia in relation to Ukraine or Iran. Separately, there is the operational information-sharing or collaboration about the commonly shared experiences of difficulties in implementation, enforcement, information-sharing and things like that.

Both those things happen. When I was there, the Commission tended to have more involvement in the latter because it has a greater role in implementation and ensuring good operation and enforcement of sanctions. For that side of things, i.e. the common experiences across regimes rather than experience specific to a particular situation, there was a formal structure. I believe that every year — it certainly still happens; I do not know exactly how frequently now — there is a EU-US sanctions workshop. Experts from both sides sit down and share experiences. Often it was a useful opportunity for the EU to explain to the US side the ins and outs of the EU procedure, what was done at EU level, what was done at Member State level and that sort of thing.

There is also a big awareness of the benefits of alignment on individual sanctions regimes, and it generates problems for businesses in particular when there is no alignment. The US way of framing its sanctions is different from the EU way. Even where there is an alignment on a particular set of objectives, it does not necessarily mean that you will see the same measures. It is true to say that, even where you see in quite a specific level of detail an agreement with the US on the types of measure, there are differences in how they are framed. You can have alignment on the general objectives, you can have alignment on the types of measure, you could in theory have alignment on the actual wording, but I do not think that ever happens.

How that happens differs from case to case. Russia is the example of closest alignment that I am aware of: there was a very conscious desire

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<sup>2</sup> Which is COREPER



early on to make sure the measures were very closely aligned, and essentially the EU and the US operated as one. Recently, though, there have been some departures from that alignment, as you say.

**Lord Risby:** You said there was this group that meets once per year. If you take Iran hypothetically, we do not quite know what the US Administration may or may not do on this matter. Given that a year is a long time in politics, when something arises that could clearly have an impact on what was a perceived agreement, presumably there is direct contact straightaway.

**Roger Matthews:** Certainly, yes. The yearly meetings are to share operational details across the board of our general experience of delivering, framing and giving effect to sanctions in the EU, their experience and how we can learn from each other.

As to the EU and the co-ordination that has to happen in advance of regime-specific political developments, the External Action Service and the Member States—prominently the UK—that are most interested would take the lead on that, but that would happen very quickly, yes.

Q43 **Lord Triesman:** This follows on from Lord Risby's question. The original question was about being likeminded. There may be a lot more dissonance and we may not be quite so likeminded as we were with the United States. In the event that understandings about sanctions policy break down, as they may be about to on Iran, how does the system cope with what is on occasion a jolt rather than a smooth change in which people can have a dialogue over a period of time?

**Roger Matthews:** The discussions on that will be political discussions. The form they will take is often an EEAS-led round of meetings, which will happen in very short order. I am probably not the best person to give the detail on how those come about. There is a confidential system in the EU whereby Member States can air ideas and you can very quickly, within a matter of hours, get a sense of whether there is a political momentum building up.

I know you have had evidence from the Foreign Office about what Matthew Findlay called the political 'head of steam'. Certainly, if there were a "jolt", that head of steam would build up very quickly. There has not been a jolt in the sense of an unexpected disparity between EU and US sanctions that I have experience to draw on, but in general terms it will be addressed in the same way as a jolt in the sense of a fresh circumstance arising that requires a new set of sanctions: it will require the same rounds of engagement between the External Action Service and the key sanctions players in the Member States, and of course outreach to the US, particularly if it is a jolt in the sense of a disparity between the two, to understand where the US is coming from and how that can best be addressed.

Q44 **Lord Horam:** We have been talking so far about how things operate now, but obviously we want to look ahead. We must assume that Brexit

will happen in March 2019. In advising your clients at the moment I presume you must have formed some preliminary view at least—hypothetical it may be—on how co-operation between the UK and the European Union might operate post-Brexit. I am thinking in particular of Russian sanctions, for example, with regard to which the UK may have a significant role, although it will differ from time to time and place to place.

**Roger Matthews:** I know the Foreign Officer representatives made the same point, as have others, that the UK has played a significant role in most of the sanctions regimes the EU has, but you are right: it is most acute in the more complex regimes.

After Brexit, yes, it is certainly important that the UK continues to have a closely aligned position with the EU. That is recognised in the Future Partnership Paper the Government have put out. How that comes about is a bit of an open question, of course. My personal view is that merely sitting outside the room and trying to influence EU decision-making, without being at the table, is valuable, but it only gets you so far. It cannot ever be a substitute for having a formal structure whereby the UK is around the table and able to influence the formal arguments.

**Lord Horam:** How far does it get us? Do you have any experience of that situation?

**Roger Matthews:** The closest experience I can think of to draw on is that of countries, such as Norway and Turkey, that do not have a seat at the EU table but from time to time have an interest. I am not aware of a time when they were able to exercise significant influence on the shape of the sanctions. They might have been informed, but I am not aware of a time when they were able to exercise any significant influence at all.

**Lord Horam:** They are perhaps not a very good example, because they may not have a very significant role to play, whereas Britain may have a significant role, for example, in financial sanctions on Russia. Would that change things?

**Roger Matthews:** Yes, that would change things. There is a question about whether the better analogy for the UK is Norway or the United States, and the honest answer is that we are probably somewhere between the two. The United States does not have a seat at the table, but everyone is very aware of what it is doing.

**Lord Horam:** How does the US communicate that?

**Roger Matthews:** It does so through bilateral discussions with Member States and through the External Action Service. By the time everyone is in the room in a working group, they are pretty aware, certainly informally and very commonly formally.

**Lord Horam:** Have you formed any view as to how the UK will look on its role post Brexit?

**Roger Matthews:** It will certainly want to carry on shaping EU sanctions. That is because, quite aside from its own sanctions, it needs to make sure that EU sanctions continue to take a path it would like them to take. While it has been at the table, the EU sanctions to a very large extent have been an amplification of the positions the UK wanted to see.

The best way of achieving that would be to have a structure whereby it can sit around the table. There are possibilities for how it might achieve that. The Common Foreign and Security Policy is generally slightly distinct from the core EU operation. Whether it could be negotiated I do not know, but it seems to me that it should be worked through as to whether it may be possible for the UK to have a formal position in CFSP even while otherwise sitting outside the EU.

An important point about the Common Foreign and Security Policy is that, with a couple of exceptions, it is outside the reach of the European Court of Justice. That is why I say it is outside the core operation of the EU. That may not work, because one of the few exceptions and one of the areas where CFSP Decisions are subject to ECJ jurisdiction is sanctions listing. This may not be possible, but it seems to me that there may be some room for a forum, which is not the forum for making Regulations but a forum at a more political level, where the UK could have a seat at the table.

The CFSP may offer that; the Political and Security Committee may offer an opportunity for that. I do not know, but it seems to me that there may be some possibility.

**Lord Horam:** That is an interesting idea. Will they have to have some institutional link?

**Roger Matthews:** It would be of massive benefit, certainly. If they do not have it, they will be in the same position as the US — in not having a seat at the table — they will find the best possible ways to make their views known, to exercise influence, to maintain the bilateral links with the External Action Service and the other Member States, and to influence that way, but it would certainly be a massive advantage to have a seat at the table in a political forum.

Q45 **Lord Dubs:** In very simple terms, I understand in theory why we would like to have a seat at the table and why we would like to have influence, but in practice once Brexit has happened would the right thing not be for us to say that we will go along with the EU sanctions? Why would we want to differ? Could you give me an example of why we would want to take a different line as opposed to automatically saying, "Okay, we will go along with this"?

**Roger Matthews:** The first point is that EU sanctions may more often take a line that we do not like if we have less influence over them. When the UK is at the table and is part of the body that decides what the EU sanctions look like—in fact, we are a very influential part of that

committee—inevitably we decide that we are happy with the result, because that is why we have gone along with it.

When we are not at the table, there is more of a risk that on occasion the UK does not like a whole EU sanctions regime, or perhaps more likely particular elements within it. Therefore, there may be more occasions when it is not comfortable to go along with it but cannot stop it.

The examples may be very specific. For example, the UK and the EU may be aligned on the need to have sanctions against a particular country and on the broad measures, but another country has lobbied very hard for a particular carve-out because it has a particular industry concern that would otherwise be very hard hit, and the UK may not be particularly interested in the UK also making that carve-out. The UK may say, "Yes, in principle we will align very closely with the EU sanctions, but we are not worried about the carve-out that has been included in the EU sanctions". Therefore, there is an exception that will be in the EU's Regulation but will not be in the UK's corresponding one. That might be an example of where we would broadly align without exactly aligning.

On a bigger-picture scale, of course there may be situations—I do not know whether this is likely; it will depend on the Government of the day—where we simply drift more towards the US position or align more closely with the US position and go for a different model completely.

**Q46 Lord Stirrup:** We are talking here about why the UK would want to influence EU sanctions policy formulation post Brexit and how it might do so, but to what extent—I am of course asking you to speculate based on past experience—will the EU will attach importance to gaining alignment with the UK in its sanctions policy? In other words, are we just chasing something that nobody else is going to be interested in, or is there a fair degree of mutual interest in finding some sort of formula that would allow us to reach that degree of alignment?

**Roger Matthews:** Like anyone else, the EU is aware of the point that was made earlier: the more countries are on board with the same sorts of sanctions against the same thing, the more effective those sanctions are. That is widely recognised. The UK is a significant economy and will continue to be, so having the UK on board in an EU sanctions regime certainly amplifies the effectiveness of that regime.

From a business point of view, there is an additional consideration: if the UK and the EU have the same sanctions, it obviously makes things operationally easier. That will be a consideration for the EU with EU businesses in mind as much as it is a consideration for the UK with UK businesses in mind. There is a benefit in both ways of harmonisation, ideally on the letter of the law, but certainly as close to it as possible.

The third element is that the EU is very well aware that sanctions are an area where the UK has taken a very prominent lead, both in framing the sanctions and in identifying individuals who should be targeted by particular measures. It will be interested in co-ordination, not only to get

the UK on board with its measures but to get UK input and assistance on how those measures should be framed. It is an area where there is a real opportunity for the UK to continue to have a constructive role and where the EU is likely to welcome that rather than resist it.

**Q47 Baroness Manzoor:** Can I come back to the US? You talked about alignment. To start with, what percentage of EU sanctions are aligned with US sanctions?

**Roger Matthews:** I would not like to put a percentage on it. To an extent it depends on what you call alignment. Russia is a good example. Until recently, they were very closely aligned. There are now a couple of measures in the Acts that the US adopted in the summer that move away a little from that alignment. They have adopted new measures, including prominently a secondary sanctions measure that might well affect EU companies, that move away from the alignment. The extent of alignment has shifted. As I said earlier, even where the general policies are aligned, often the actual application of those policies means there are differences in the measures businesses have to take to ensure compliance with both.

There are a few—I could not put a percentage on it—where either the EU has acted without any corresponding US action or the US has acted without any corresponding EU action. On the US side, Cuba and Venezuela are two prominent ones at the moment. Whether they are the only ones, I could not be sure, but they are prominent ones. On the EU side, there are only a small handful, but there are certainly some. They are minor regimes, not in the sense that they are unimportant but in the sense that the EU measures extend to an asset freeze for a very small number of people and perhaps an arms embargo but do not go very much further than that. There is a degree of alignment on all the major sanctions regimes.

Of course, Iran is probably the elephant in the room when it comes to alignment. Yes, we both have measures in relation to Iran, but since January 2016 the nature of our measures has been very different. I do not know whether you would say there is alignment because we both continue to have some measures against Iran, or whether you call it non-alignment because they are very uneven.

Those situations can cause a bit of a problem. They cause a big problem for businesses, because businesses do not follow the detail of what happens. They follow it at a step that is slightly removed and commonly have misperceptions about the extent to which EU and US sanctions are aligned. Sometimes they think wrongly that there are no longer any EU sanctions, and sometimes they think that the EU and the US have the same sanctions when in fact they do not. Non-alignment causes problems, but there are not very many cases of complete non-alignment.

**Q48 Baroness Manzoor:** Coming back to OFAC, when the political decision has been made, does the EU contact the US, look at its Regulations and then work very closely together with it? Is that the process? What is the process?

**Roger Matthews:** When I worked at the Commission, it was not at that level of detail. In the more recent case of Russia in particular, I understand that the EU and US worked very closely to make sure that the measures were very closely aligned, but even there the measures are not the same. The lists of targeted entities are different. There are entities on the US list that are not on the EU list.

Then there are myriad very minor variations, such as precisely how the energy sector impact or the financial sector impact operates, or whether an entity that is exactly 50% owned by a listed entity is caught by the sanctions. They are technical differences, but they all count for the businesses affected by them.

When you are framing it, it is safe to say that the more you are going to align the elements, the more you would like that alignment to go down to the operational level so that there are as few specific differences as possible.

**Baroness Manzoor:** Can you give some examples? I am struggling to understand. You are saying that EU sanctions are very much aligned with US sanctions. There are variations in some of the Regulations, but can you give any key examples of great differences other than on Russia, Ukraine and Cuba?

**Roger Matthews:** There are great differences on a lot of sanctions regimes. For Iran, there are great differences because the EU has chosen to lift most of its sanctions, whereas the US has chosen to retain most of its sanctions but to reduce only the lists a little and lift its secondary sanctions. With Iran, there is a very different situation: US persons basically cannot operate in Iran; EU persons can operate in Iran but with some restrictions on exports and on particular people they may not deal with.

I could run through quite a long list of sanctions regimes where there are individual differences. Until two weeks ago, there was a very significant difference on Sudan between the extent of the US and the EU sanctions. The EU lifted sanctions on Sudan a number of years ago. The US suspended them a few months back and then eventually lifted them only two weeks ago.

Russia is the opposite. Although I picked on the Russia sanctions earlier because there had been a concerted effort to align the individual measures but one that does not go to the level of every specific being the same, it is probably a good example of the two being very closely aligned. The norm—outside the UN context, of course; the UN has framed what UN members have to do—is for there to be a little more differential than that.

Some of that difference between US and EU measures comes down to a cultural difference in how sanctions are structured. I hope I am not overgeneralising here, but the US's general approach to its more complex—its term is "comprehensive"—sanctions is to start by saying,

"US persons may not deal with this country", but then to row back from that with a series of general licences. They say, "US persons may not deal with Syria, but here is a general licence for medical products, here is a general licence for humanitarian aid", and so on. EU sanctions are framed the opposite way; they start from the point of view that everything is allowed save where there is a prohibition or restriction saying that it is not allowed. Although the EU has very complex and extensive sanctions on Syria, it does not say, "EU persons may not deal with Syria". It says, "You may not invest in Syrian businesses in these sectors. You may not deal with these people. You may not export these products".

The cumulative effect of all those individual restrictions is not very different from the US blanket ban with general licences, but it is a very different approach. Therefore, it is not really workable, when framing or putting together a new EU sanctions regime, to look across to what the US does, because its sanctions are structured in a very different way, even if the objectives are quite similar.

- Q49 The Earl of Oxford and Asquith:** Following on from that, perhaps you could comment on the various processes of enforcement of sanctions. Are there significant liaisons between EU Member States or between a Member State and the Commission? You have touched on Iran a couple of times. Perhaps that is not the right question. Perhaps the question is more about whether those significant interactions are between corporate sectors. For example, the financial sector in Iran seems to me to be one of those sectors where there are not so much different enforcement rules in place, but very different practices.

**Roger Matthews:** Do you mean very different between EU Member States?

**The Earl of Oxford and Asquith:** I mean between various players in the corporate sector, between various banks, whether in Germany or Switzerland—although Switzerland is not part of the EU, obviously.

**Roger Matthews:** Let us start with the formal enforcement structures. The first important thing is to make a distinction. For implementation, there is a bit of a pan-European role for the Commission, as a guardian of the Treaties, that has an interest in ensuring consistent interpretation and application of EU law throughout the EU. The Commission has a role at the implementation stage. For example, it recently issued a Question-and-Answer document on Syria sanctions to help to ensure a consistent application. That is different from enforcement. Enforcement is done at the Member State level. You had representatives from the Office of Financial Sanctions Implementation here a few weeks ago. It is the UK's competent authority, and each other Member State has a corresponding competent authority. Enforcement is down to OFSI.

There is a provision in each EU Regulation that says that each Member State has to have effective, proportionate and dissuasive penalties, but that is as far as the EU goes. It is down to the Member States when

framing their national laws to decide what is an effective, proportionate and dissuasive penalty and to decide what powers to give their enforcement authorities to ensure there is the possibility of doing enforcement and issuing those penalties.

It is useful to look across to the US, although they do not have the issue of EU-level versus Member State level, and I note that their enforcement overall has been a lot more aggressive and a lot more prominent, with very high fines, in a way that you simply do not see in the EU. On the EU side, there have been a handful of convictions and penalties for breaches of the trade aspects of sanctions, such as companies illegally trying to ship goods to Iran, for example, which happened not very long ago. But there have not been, to my knowledge, any significant enforcement actions in any EU Member State for breaches of the financial sanctions.

That said, the UK has given OFSI a good suite of powers with respect to both criminal enforcement and the possibility of issuing civil monetary policies for breach of sanctions, which is a very valuable tool. It only got that power earlier this year. It has not started using it yet, but I am sure it is only a matter of time. At least as far as the UK is concerned, I expect we will see enforcement becoming a more prominent part of the way sanctions are given effect.

In other countries I am not aware of a similar beefing-up of formal powers, but I know that other EU countries are beginning to take enforcement a bit more seriously. At the moment it has been very one-sided. It looks from the outside as though OFAC is lashing out vast penalties and the EU is being a bit quiet. We are not going to go to the OFAC level, but we expect to see the UK in particular, but other EU Member States as well, being a bit more active on the enforcement scene.

When you come to the perception of banks in particular and other financial services operators, of course a lot of these entities are global players anyway. It is true—we see this very much from where I am now at Dechert—that while businesses certainly care about EU sanctions and take them very seriously, their biggest concern is the US sanctions, because they know that OFAC is very aggressive, the fines are very high and the public censure is very serious. They see it much more as a genuine risk, so that is something that drives their concerns.

Therefore, when you look at how that plays out in a context like Iran, where the US sanctions are much more onerous than the EU sanctions, you will very commonly find banks saying, 'We are not interested in having a policy that allows things to be done in the EU that are legitimate under EU law if there is even the slightest risk of us engaging the US jurisdiction and being subject to very hefty US fines'. They may not put it that way, but that is the underlying thinking.

They tend to err in favour of the safe option of simply not doing business, or not doing most business, with countries where there is even the vaguest risk of a US jurisdictional issue. The problem is that US



jurisdiction is very wide, so the banks tend to have policies that discourage accepting any business with Iran and that sort of attitude.

- Q50 **Lord Dubs:** After Brexit, would you expect there to be a change in the way sanctions are enforced in the UK? We have the Sanctions Bill coming along. What would the implications be for listed individuals and entities?

**Roger Matthews:** I do not think a lot will change in enforcement. OFSI has its suite of new powers. Because enforcement has always been a Member State competence rather than an EU-level competence, that specifically will probably not change very much. We will see a change because it will gradually develop familiarity with how best to use its new powers, but that will not be a change that is brought about by Brexit particularly.

On the question of the impact on listed persons and entities, yes, there will be a difference. Exactly how that difference plays out we will have to see when the Sanctions Bill is published. From the White Paper that has been published so far, we can see there is a recognition of the value of having listing criteria that are broadly similar to other Member States and having evidential thresholds that are broadly similar to other countries. That is certainly helpful.

One issue that is likely to arise is that a listed person's basis for their listing in the UK will be legally independent of their basis for listing in the EU. I suppose a listed person might see this as an opportunity to have two bites at the cherry in challenging its listing. At the same time, they will be able to challenge it through another Member State and up to the EU courts, and through the UK and the UK courts system. I suppose the downside for them is that to be fully delisted they would have to succeed in two different fora, so you could look at it both ways. The merits of that will depend on the individual listing, but that is the key implication.

- Q51 **Baroness Armstrong of Hill Top:** Mr Matthews, I just wanted to explore a little more the effect on businesses of the anticipated changes with Brexit. What will the advantages and disadvantages for businesses be in the future? You have said something already about the difference between how they approach the US sanctions regime and the EU regime. How are they thinking about this issue?

**Roger Matthews:** Within the EU, you can see a number of key advantages to the current system. One is that, while it is not a perfect system, it is nonetheless familiar. Businesses have found a way to work with it. Therefore, switching to any different system in a sense is going to bring some transitional issues. That is probably not the main issue, but that is perhaps the first point to make.

The second point is a wider extrapolation of that. There is a value for businesses in harmonisation. This point is not confined to sanctions, but it is certainly true of sanctions. Businesses have their compliance procedures. They are tailored to comply with EU sanctions. Most of our clients at least—this is true of a lot of businesses that are affected by sanctions—are not going to be one-country businesses. They are not

going to deal only with the UK. They probably have operations in other EU countries as well. So in any case, they will have to continue to have compliance policies that take account of EU sanctions.

It is not as if a business is going to say, "Maybe the UK sanctions will be better than the EU ones or maybe they will be worse. We will switch to comply with the UK ones". They will have to do both. They will have to comply with the UK sanctions on top of complying with EU sanctions. Therefore, if the UK and EU measures are anything other than very closely aligned, the compliance implications of that are an added cost for businesses.

Finally, the other obvious advantage of EU membership relates to licensing. For some of the financial sanctions licences, you have to go to different competent authorities if you have significant activity in different EU Member States. But for export licences, for example, if you are exporting an item from the UK to Finland, for example, and then on to Russia, your UK export licence could carry the whole of that, whereas obviously if the UK and Finland, in my example, are not in the same framework, there will be a need to apply to two separate authorities for licences. Again, it is an operational burden. How big an operational burden will depend on the different countries involved. It will hit physical exporters particularly hard as against the current system, but the exact nature of it will depend on how things are agreed.

One disadvantage of the current system that we touched on a little earlier is that often the drafting of EU Regulations is a bit of a compromise. That compromise will sometimes involve restrictions or exceptions that another country has insisted on, or something that the UK would not be bothered about or perhaps would actively not want. Sometimes businesses might prefer to have a Regulation that did not take account of a compromise with another country. The UK can have sanctions that are more tailored to UK concerns, including UK businesses' concerns. That will not always work in favour of businesses, of course, but it might do in some cases.

The other obvious advantage is something that OFSI flagged up in earlier evidence. At the moment, I understand that OFSI feels a bit hampered in the extent to which it can give clear guidance, because it is very conscious that it is being asked to advise on EU law and it has to take account of the positions of other EU Member States. Ultimately, EU law is decided by the ECJ, and if UK sanctions are independent we might get clearer guidance from OFSI.

At the moment, one of the problems is that sanctions are not drafted in a very detailed way. Having been a draftsman, I know there are good reasons for that, but I appreciate that it causes problems for businesses. If we can get some clearer guidance from OFSI as to how those should be applied in different sectors, that would be of fantastic value to businesses. I am hoping that is something that might come out of it.

**Q52**     **Baroness Suttie:** To a fairly large degree you have already covered this

question, but, as far as you are aware, what assessment have businesses based in the UK done on the impact of complying with a UK-only sanctions regime?

**Roger Matthews:** I am not aware of a specific assessment of the impact for the simple reason that it will be very hard to say how different it is until we learn a little more about it. As I just said, one thing I am conscious of is that while the question that was put in advance to me was about a UK sanctions regime as opposed to an EU sanctions regime, that is not actually how businesses tend to see it. They will see it as having to continue having awareness of the EU sanctions anyway, and for a lot of them also of the US, and then there will be the UK measures in addition. By and large, they are looking at it from that perspective.

Of course, we will only know the extent of the added cost when the Sanctions Bill comes forward. In addition, it is worth saying that the Sanctions Bill will tell us useful general things such as the UK's policy on licensing, which I gather is one area where we might get a bit more flexibility for UK licensing authorities than the EU, and a few other general points. It will not tell us—this will only come about on the politics of any particular regime—whether on any particular regime the UK aligns closely with the EU position, the US position or goes its own way. For each regime, the choice the UK Government make on that at the time will affect the burdens of having to comply with the UK separately from the EU.

**The Chairman:** Thank you very much, Mr Matthews. That has been an exceptionally detailed and comprehensive session this morning. I, for one, have really appreciated your being here. It has made us think very clearly about some of the greater issues that will come forward. Thank you very much. I will once again repeat that the transcript will be sent to you. If there are any corrections, please let us have them back. I draw the public meeting to a close, so thank you very much.