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Submission to the Senate Foreign Affairs, Defence and Trade Reference Committee's Inquiry into Australia's sanctions regime

23 September 2024

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To Foreign Affairs, Defence and Trade Reference Committee

Date 23 September 2024

1 Introduction

Thank you for the opportunity to make this submission in response to the Senate Foreign Affairs, Defence and Trade Committee's inquiry into Australia's sanctions regime.

Allens has a long history of representing many of Australia's largest companies in regulatory investigations, civil penalty proceedings and criminal prosecutions. We also have extensive experience advising domestic and international clients on the effect of Australia's trade and financial sanctions and export control regimes in compliance, transactional and investigations contexts. We are familiar with foreign sanctions regimes, including those of the United Kingdom, European Union and the United States.

We therefore consider that we are well positioned to provide valuable insight into the operation of Australia's Sanctions regime and welcome the chance to contribute to its continuing development.

We have responded to items (a), (b), (e), (g), (h) and (i) of the Terms of Reference below. Several of our submissions reflect those we made to the Australian Sanctions Office (***ASO***)'s review of Australia's Autonomous Sanctions Framework in March 2023 (***ASO Review Submissions***).[1]

2 Consistency in application of Australia's sanctions regime and in coordination with key partners and allies

Australia regularly aligns its sanctions programs with those imposed by key foreign allies, particularly the European Union, United Kingdom and United States. However, even when it does so, due to differences in the sanctions law framework of Australia and its key foreign allies, Australia's sanctions programs may have substantially different applications to comparable programs of key allies and therefore may have significantly different consequences. In our experience, this creates material difficulties for Australian companies, as well as Australian citizens employed for foreign entities, and can impact their ability to compete globally. As sanctions are most effective when they are consistently and widely adopted, we consider that Australia's sanctions law framework should be aligned – so far as is possible – with those the European Union, United Kingdom and particularly the United States (as the jurisdiction that most actively imposes sanctions and enforces sanctions laws).

We have discussed below the key inconsistencies in the Australian sanctions regime that would benefit from alignment with comparable foreign regimes.

2.1 Targeted financial sanctions - lack of clarity on application to entities partially owned or controlled by sanctioned persons

A primary inconsistency between Australia's sanctions regime and those of key partners is that Australia does not apply a brightline rule when assessing whether targeted financial sanctions flow through from a designated person to another entity. For example, the 50% rule is a feature of the sanctions frameworks of the European Union, United Kingdom and United States. Though it takes differing forms, the 50% rule generally provides that if a designated person owns 50% or more of an entity (or additionally in the case of the European Union and United Kingdom,

[1] Available at https://www.dfat.gov.au/sites/default/files/review-australia-autonomous-sanctions-framework-submission-allens.pdf.

exercises certain forms of control over an entity), that entity is also considered to be a designated person.

The absence of a brightline rule in Australia creates uncertainty as to when sanctions flow from a designated person through to their related entities. This in turn creates significant compliance challenges for Australian companies, and means that many conclude that they are unable to enter transactions in circumstances where their American, British and European peers who are subject to similar sanctions programs might conclude that they are able to do so.

Consequently, we submit that Australia should adopt a brightline rule regarding the application of targeted financial sanctions to entities partially owned or controlled by sanctioned persons.

2.2 Import sanctions – global application

Another primary inconsistency between Australia's sanctions regime and those of key partners is that Australian import sanctions have a uniquely broad application.

The 'import sanctions' label is something of a misnomer – as well as prohibiting the import of sanctioned products, this category of Australia sanctions also prohibits Australian individuals and companies from purchasing and transporting them. On a plain reading of relevant legislative instruments, and as recently confirmed by the Federal Court of Australia in *Tigers Realm Coal Limited v Commonwealth of Australia* [2024] FCA 340, these prohibitions apply globally, not just when a relevant transaction has a physical nexus to Australia. European Union, United Kingdom and United States import sanctions do not have a similarly broad application.

In some sectors, this places Australian businesses at a critical disadvantage. For instance, some liquid fuel products are distributed from bunkers in third countries that are regional or global transportation hubs. Some of these countries do not impose sanctions programs that are equivalent to those imposed by Australia. As a consequence, local suppliers in these countries may not be prohibited from receiving liquid fuel products that Australia imposes sanctions on into their bunkers (like Russian refined products), and Australian companies operating offshore may not be able to utilise these bunkers without assuming exposure to Australian sanctions laws, even in circumstances where they have no viable alternative suppliers.

We submit that Australian import sanctions should not apply more broadly than those of Australia's key allies. For instance, it could be appropriate to clarify that they only apply if a transaction has a physical nexus to Australia. Further, we consider that this application of Australian sanctions does little to advance Australian foreign policy objectives, particularly in circumstances where Australian corporations lack the market power to affect the purchasing behaviour of foreign counterparties.

2.3 Lack of winddown period

The Office of Foreign Assets Control (***OFAC***) provides a 90 day wind-down period under some sanctions to allow persons engaged in transactions which could be sanctioned under new sanctions designations to take necessary steps to wind down those transactions. To minimise harm to Australian businesses when a foreign corporation that has financial or trading relationships with Australian counterparties is designated as a sanctioned person, we submit that the Australian sanctions regime should include wind-down periods similar to those provided by OFAC. The provision of a wind-down period would allow a short window for Australian businesses to negotiate contract terms, manage inventory and ensure that Australian consumers are not affected by the designation of counterparties. We consider that such a period would be of particular utility in circumstances where autonomous sanctions are introduced by Australia but not yet been introduced by key allies.

2.4 Liability mechanisms – Lack of a civil liability mechanism

A final inconsistency between Australia's sanctions regime and those of key partners is that Australia lacks a civil liability mechanism. As we submitted in response to the ASO's review of Australia's Autonomous Sanctions Framework in March 2023, we consider that there may be benefit in expanding the regime to provide for civil enforcement, as well as criminal enforcement.

The current Australian corporate sanctions offence is one of strict liability (i.e., there is no fault offence), and the offence may occur in the case of a minor one-off breach or an isolated incident where an automated system or process inadvertently fails. We do not consider that the public interest would warrant a criminal prosecution in such circumstances. By contrast, where a civil liability mechanism exists there is greater latitude to investigate and take regulatory action in respect of conduct which has arisen in the context of a risk management failure. Taking enforcement action under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (***AML/CTF Act***) as a comparator, we consider that civil penalty proceedings (and associated enforcement mechanisms such as enforceable undertakings and external audits) by AUSTRAC have led to an increased focus on AML/CTF compliance and investment in AML/CTF compliance by Australian corporations.

In a sanctions context, as in the AML/CTF regime context, we consider that a risk management failure is the most likely circumstance in which a corporate entity may breach the regime, and so we consider the AML/CTF Act is an apt comparator. In this context, consideration might be given to the introduction of civil consequences for minor, isolated, or non-systemic breaches, such as infringement notices or remedial directions. Any criminal offence can then be left for conduct which involves an element of intent and which more readily warrants criminal prosecution.

The introduction of a civil penalty regime would bring Australia in line with its key foreign counterparts. For example:

- the US imposes criminal penalties for 'wilfully' violating US sanctions, and has a civil penalty regime for other types of breach which do not involve that element of intent; and
- similarly in the UK there is a criminal offence available where there is some element of intent, but there are also civil enforcement powers which are available in other circumstances.

3 Opportunities for engagement

The ASO is Australia's primary sanctions regulator. It is important that the ASO is approachable and can provide assistance and support to Australian companies considering and managing sanctions compliance challenges in a timely manner. We welcome the increased resources provided to the ASO's budget in the 2024-25 Budget and consider it important that its funding levels are maintained and expanded over coming years to enable it to support Australian companies' compliance efforts. In particular, we submit it is important that the ASO is given sufficient resources to:

- increase outreach efforts and consult across relevant sectors about the impacts of Australian sanctions, so that it may remain abreast of the most significant impacts from the perspective of industry, develop relevant guidance, and improve the overall effectiveness of Australia's sanctions regime in practice;
- process permit applications expeditiously and within commercial timeframes; resume issuing indicative assessments, which are ASO assessments of whether a proposed activity is permitted by Australian sanctions, and which are valued by the private sector; and

- improving the utility of the consolidated list, to ensure it is workable and accessible for regulated entities.

In our view, Australian businesses would benefit from the release of publicly issued guidance by the ASO to assist with understanding how to comply with sanctions laws effectively and reduce the risk of inadvertent breaches. Guidance from the ASO would assist to promote consistency in how sanctions are applied and enforced across sectors and bring the ASO in line with equivalent sanctions regulators, such as the Office of Foreign Assets Control in the US and Office of Financial Sanctions Implementation in the UK. Specifically we consider that businesses would benefit from guidance on the sanctions defence of reasonable precautions and due diligence.

4 Opportunities for alignment with anti-corruption and crime measures

We consider that greater alignment between the sanctions regime and Australia's AML/CTF regime and recent reforms to the foreign bribery offences under the *Criminal Code 1995* (Cth) would benefit Australian businesses who have exposure to the sanctions regime.

In relation to opportunities for alignment between Australia's sanctions and AML/CTF regimes, we understand that the *Anti-Money Laundering and Counter-Terrorism Financing Amendment Bill 2024* proposes to require reporting entities to establish on reasonable grounds whether a customer (or the agent / beneficial owner of a customer) is a designated person under targeted financial sanctions before commencing to provide a designated service. In our experience reporting entities have been precluded from engaging with customers in relation to sanctions compliance issues as a result of the operation of the AML/CTF Act tipping off offence.[2] As the Consolidated List and sanctions designations are public information, we recommend consideration be given to a whether suspicions related to sanctions offences be excluded from the ambit of s123 of the AML/CTF Act. Such a carve out would have two clear benefits:

- First, it would allow reporting entities to engage with customers to understand the sanctions risks which those customers pose; and
- Second, it would allow reporting entities to provide a clear reason to customers who are exited as a result of sanctions designation.

We also consider a protection from liability provision similar to section 235 of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) and section 44 of the *Sanctions and Anti-Money Laundering Act 2018* (UK) should be considered for inclusion in Australia's sanctions regime. This would provide protection for a person who has acted in the reasonable belief that they are complying with sanctions.

In relation to opportunities for alignment between Australia's sanctions and foreign bribery laws, the similarities between the failure to prevent foreign bribery offence introduced by the *Crimes Legislation Amendment (Combatting Foreign Bribery) Act 2024* and the corporate sanctions offence mean that any guidance issued by the ASO regarding compliance requirements should be generally aligned with the principles set out in the Attorney General's Department Guidance on Adequate Procedures to Prevent the Commission of Foreign Bribery, that is guidance should be principles based and recognise the importance of proportionate controls.

5 Other matters

5.1 Mental element for the natural person sanctions offence

One additional matter that we would like to raise is that the application of the natural person sanctions offence is unclear on the face on the sanctions legislation and should be clarified.

[2] AML/CTF Act, s123.

The sanctions legislation does not set out the fault element that applies to the natural person offence. Consequently, it is necessary to read the offence in light of Part 2.2 of the *Criminal Code* (Cth). This is not a straightforward exercise.

The interaction of these statutes has been judicially considered by the Supreme Court of New South Wales in *R v BB*,[3] in which it was held that for an individual to breach an Australian sanction they must both:

- intend to engage in the relevant conduct that breaches the sanction; and
- know or be reckless as to whether the relevant conduct breaches the sanction.

In our view, to promote understanding of the application of Australian sanctions, this position should be codified in the sanctions legislation.

5.2 Application to Australian expatriate employees of foreign companies

One further matter that we would like to raise is that Australian sanctions laws can have an unduly harsh application for Australian expatriate employees of foreign companies.

We have received a considerable number of enquiries concerning the application of Australian sanctions to expatriate Australian persons who are employees of foreign companies that are outside Australian jurisdiction.

The primary issue is whether an Australian employee who contributes to a corporate action taken outside Australia that might breach an Australian sanction were that corporation within Australian jurisdiction is at risk of breaching that sanction. The issue is highly significant in circumstances where the home jurisdiction of the foreign corporation and/or the jurisdiction in which the Australian expatriate employee is based does not have in place sanctions that are equivalent to an Australian sanction.

At present, there is no direct statutory or regulatory indication of the level of employee involvement in a corporate action that might amount to a breach. As a consequence, to shield Australian expatriate employees from potential exposure to criminal liability, some foreign companies have restructured or reduced Australian expatriate employees' roles. Such compliance measures can have significant personal and professional implications for individuals.

As such, clear guidance on whether and when an employee's contribution to a corporate transaction rises to the level that they themselves will be said to have engaged in relevant conduct would be helpful. In our view, a strict standard based on the identification doctrine should be applied. That is, an Australian expatriate employee should not be liable for the conduct of a foreign corporation outside Australian jurisdiction unless corporation is acting as alter ego of the employee.

[3] [2019] NSWSC 1054.