House of Commons

Treasury Committee

Defeating Putin: the development, implementation and impact of economic sanctions on Russia: Government Response to the Committee's Twelfth Report of Session 2021–22

First Special Report of Session 2022–23

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The Treasury Committee

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Committee reports are published on the Committee's website at www.parliament.uk/treascom/ and in print by Order of the House.

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The current staff of the Committee are Morenike Alamu (Committee Operations Officer), Rachel Edwards (on secondment from the Bank of England), Kenneth Fox (Clerk), Dan Lee (Senior Economist), Adam McGee (Senior Media and Communications Officer), Aruni Muthumala (Senior Economist), Moyo Oyelade (on secondment from the Bank of England), Charlotte Swift (Second Clerk), Ben Thompson (on secondment from the National Audit Office), Sam Upton (on secondment from the Financial Conduct Authority), Adam Wales (Chief Policy Adviser), Maciej Wenerski (Committee Operations Manager), and Marcus Wilton (Senior Economist).

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You can follow the Committee on Twitter using @commonstreasury.

First Special Report

The Treasury Committee published its Twelfth Report of Session 2021–22, Defeating Putin: the development, implementation and impact of economic sanctions on Russia (HC 1186), on 23 March 2022. On 25 May 2022 we received a letter from the Economic Secretary to the Treasury containing the Government Response. Both the letter and the Response are appended below.

Appendix: Government Response

Letter from the Economic Secretary to the Treasury, and attached Government Response to the Report

I am writing in response to the Treasury Committee's report, '*Defeating Putin: The development, implementation and impact of economic sanctions on Russia*',[1] published on 23 March 2022. I would like to thank the Committee for the report, its support for the government's immediate response to Russian aggression, and for the recommendations it makes in a number of specific areas. Responses to specific recommendations are set out in the annex to this letter, noting that this remains a fast-moving situation.

I would like to take this opportunity to reaffirm that the UK and its international partners stand united in the face of Russian aggression towards Ukraine. In lockstep with our allies, we have introduced the largest and most severe economic sanctions that Russia has ever faced, to help cripple Putin's war machine. These coordinated sanctions will go deeper, broader, and sharper in punishing the reprehensible actions of Putin and the Russian government.

The government is starving Russia's access to finance—with asset freezes on major banks—including Russia's largest bank, Sberbank. We have sanctioned Russia's major banks with global assets worth £940bn pre-invasion. Over 3 million Russian companies are now barred from raising money on UK capital markets. With our allies in the G7, we have removed selected banks from SWIFT and we have denied Russia's entitlement to Most Favoured Nation tariff access on many products which will affect over £2.4bn worth of UK imports from Russia. As a consequence of these actions the Russian state cannot raise funds in the UK.

We are cutting off funding to Putin's war machine, freezing over 60% of Russia's foreign exchange reserves—taking $275bn out of Putin's war chest. We are going after Putin's corrupt cronies and key businesses directly—with over 1600 individuals, entities and subsidiaries designated since invasion under the Russia sanctions regime. This includes over 100 oligarchs, and their family members, with a net worth in excess of £200bn.

These sanctions and economic measures are working. I note that the Committee's report provides a detailed breakdown of how we can expect the Russian economy to be impacted by the sanctions and measures being taken (paragraphs 27–41). The government agrees that the measures taken by the UK and our allies are having a significant economic impact

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on Russia, noting that Putin himself has acknowledged the "problems and difficulties" caused by sanctions. Current estimates are that two thirds of assets available to the Russian government have been frozen, strangling access to funding for military aggression.

The government will continue to look for ways to broaden, deepen, and sharpen the measures we are taking. We are united with our partners in the G7 in our determination to bring this war to an end. And, together, we will encourage the widest possible set of countries to act with us, with a focus on those who can have the biggest impact on Putin and his war machine. Our aim remains clear: Putin must lose in Ukraine. And we will do everything we can to ensure that happens.

JOHN GLEN

25 May 2022

Annex: HM Treasury's responses to the report's recommendations

The Government must, as a priority, ensure that its guidance is clear, precise and readily available, to allow the effective implementation of sanctions across the private sector. (Paragraph 49)

We note the report's comments on the provision of guidance by the Office of Financial Sanctions Implementation (OFSI). OFSI has a suite of guidance products that ensure effective sanctions compliance across the private and charitable sector. These include General guidance on financial sanctions, Monetary Penalty guidance (OFSI's enforcement approach), Guidance for Import / Export industry, Charity Sector guidance, and Maritime / Shipping guidance. OFSI also publishes detailed guidance on sanctions regimes which contain more complex restrictions, including Russia.

This guidance reflects the extensive outreach and engagement OFSI has across industry, which has intensified since the start of Russia's invasion of Ukraine. This regular and in-depth engagement has long allowed OFSI to produce accessible guidance that is widely used in answering the most common compliance questions and raising the standard of best practice with sanctions regulations.

Such regular, detailed engagement with industry also allows for barriers to implementation to be raised quickly, and where possible, to be addressed in new or amended guidance. One such example since the start of the conflict was the issuance of guidance on how industry should treat the 'aggregation' of different designated persons' holdings in a company. This update has been singled out as extremely helpful by the trade body of the UK's financial industry, some of the largest global banks, and has reduced the overall number of enquiries around this issue.

OFSI also rapidly updated its regime specific guidance on Russia shortly after the start of the invasion. This update details the numerous additional measures the UK imposed in response to Russia's aggression, including the new restrictions on money market instruments and securities being made available to the Government of Russia. A further update will be published shortly, which will include answers to questions posed in a Cross-Government webinar OFSI jointly hosted on Russia sanctions, which had over 4000 attendees from across the private sector.

All guidance updates are broadcast to those signed up to OFSI's 'E-alerts', which currently has over 32,000 subscribers. In addition to formal guidance documents, OFSI also produces guidance though the use of informal blogs. The two blogs produced by OFSI entitled 'Russia: What has changed and what do I need to do', and 'Chelsea Football club: what you need to know' have been the two most widely read blogs in OFSI history, with the latter being quoted in national and international business and sports media publications.

The Government is right to see economic sanctions as a critical weapon in resisting Putin's war. As such the Government needs to consider increasing the Office of Financial Sanctions Implementation's resources without delay and to provide surge capacity in the form of staff with appropriate expertise. (Paragraph 50)

We note the report's recommendation to consider increasing the capacity of the Office of Financial Sanctions Implementation (OFSI). The government can assure the committee that it will continue to ensure that appropriate resources are in place to ensure our sanctions regime is effective.

OFSI has already increased significantly in scale since its inception in 2016, reflecting changes to the depth and breadth of its work on financial sanctions in that time. In light of the recent developments in Ukraine, OFSI has been instrumental in supporting the introduction of the largest and most severe package of economic sanctions that Russia has ever faced. The Treasury has swiftly reprioritised work and resources to provide additional support to the teams involved in this work, as well as establishing a temporary new Director-led co-ordination unit to provide oversight of the overall economic response and impact. We are also recruiting additional permanent staff to OFSI, which is expected to at least double in size over financial year 2022/23.

We recommend that the Government take a watchful approach to how cryptocurrencies are used to potentially evade sanctions, and ensure it has the knowledge and expertise to effectively monitor developments in this area. (Paragraph 53)

The government recognises that cryptoassets have the potential to be used to evade sanctions and that we must remain vigilant to that risk. Since January 2020, crypto-asset firms operating in the UK have been subject to the Money Laundering Regulations, and the government has also consulted on implementing the Financial Action Task Force's Travel Rule for transfers of crypto-assets.

As the report notes, on Friday 11 March the government published a joint statement from OFSI, the Financial Conduct Authority and the Bank of England on cryptoassets reiterating that economic sanctions apply to cryptoassets like any other assets and that all UK financial services firms, including the cryptoasset sector, are expected to play their part in ensuring that sanctions are complied with. It also sets out guidance for crypto firms on steps they can take to reduce the risk of sanctions evasion and sets out examples of 'red flags' they should look for when undertaking their business. This follows a statement by all G7 leaders on 11 March setting out our joint commitment to crack down on the circumvention of sanctions, including via cryptoassets.

Regulatory authorities continue to closely monitor the potential scale and nature of sanctions circumvention via cryptoassets in the UK and will not hesitate to act where required. The government is continuing to work with the regulators and international partners to ensure that sanctions are effective and enforced and are also actively exploring further steps that could be taken to help prevent any possible evasion of sanctions via cryptoassets.

As the Government moves forward with its sanctions strategy, it must take further action to support UK households, in particular those on lower incomes, to manage the subsequent rise in energy and other costs. (Paragraph 77)

The Committee acknowledges that sanctions will carry an economic impact for the UK. The government recognises that effective sanctions will involve some cost. However, we share the view of Committee that the cost of failing to take strong action against aggressive Russian behaviour would have been far higher (paragraph 76).

We recognise the pressures UK households, in particular those on low incomes, are facing meeting the cost of living. We are listening to people's concerns and are taking action worth over £22 billion in 2022–23 to help with the cost of energy bills and to ensure people keep more of their money. This includes cutting the Universal Credit taper rate and increasing work allowances, freezing alcohol duty and cutting fuel duty, a £9 billion energy package announced in February 2022 and £500 million to help vulnerable households with the cost of essentials through the Household Support Fund. At the Spring Statement 2022 we went further, and announced an increase to the annual National Insurance Primary Threshold and Lower Profits Limit to £12,570, a cut to fuel duty, and an additional £500m to help with the cost of essentials through the Household Support Fund.

On average, the poorest households have been protected the most by government decisions since the 2019 Spending Round (SR19). Distributional analysis published at the Spring Statement showed that, on average, the combined impact of personal tax and welfare decisions made since SR19 is progressive, placing the largest burden on higher-income households as a proportion of income.

Our modelling shows that the poorest 60% of households receive more in public spending than they contribute in tax, and households in the lowest income decile will receive more than £4 in public spending for every £1 they pay in tax, on average. In the longer-term, the government is maintaining its focus on helping people back into work, which is the best strategy to sustainably reduce poverty and support those on low incomes. The government's Plan for Jobs is helping people into work and giving them the skills they need to progress—the best approach to managing the cost of living in the long term.

The government continues to keep this situation under review, recognising the high level of current uncertainty—including monitoring the ongoing impact of Russia's invasion of Ukraine on the economy—and will be ready to take further steps here if needed to support households.

The Government should consider what steps can be taken to boost business investment and growth and specifically how it can help firms which have been directly affected by the economic sanctions against Russia (Paragraph 78)

We note the report's contents, and the Committee's recommendation, regarding the impact on businesses. The government seeks to ensure sanctions measures are carefully targeted and avoid unintended consequences. For firms directly affected by economic sanctions, the Department for International Trade has expanded its Export Support

Service (ESS) to act as a single point of enquiry for businesses and traders with questions relating to the situation in Ukraine and Russia. Any business that has questions about trading with Ukraine or Russia, can visit https://www.gov.uk/ask-export-support-team, or call the relevant helpline. DIT will continue to support business and traders during this period with a dedicated export support team ready to help at the end of the phone, ensuring business can access the information they need at any time.

More broadly, we are continuing to look at ways to boost business investment and growth. Our Plan for Growth, published last year, set out the government's plans to increase investment in three pillars of economic growth: capital, people and ideas. The government has already taken important steps to meet its commitments to growth, such as through the landmark capital uplift at Spending Review 2021, and plans to invest £20 billion per year in R&D by 2024–25.

We have also brought forward measures to encourage business investment. For example, under the super-deduction, companies have until the end of March 2023 to make qualifying plant and machinery investments on which they can claim a 130% capital allowance. It is the biggest two-year business tax cut in modern British history. We have also extended the temporary £1 million annual investment allowance level until the end of March 2023.

As set out by the Chancellor in the recent Mais lecture and at Spring Statement 2022, in order to lift our growth and productivity we also need the private sector to invest, train, and innovate more. This requires a competitive and stable tax system which provides business with the confidence to invest and grow. The government recognises it can support this aim by providing clarity and certainty over the long-term development of different aspects of the tax system. Accordingly, we set out the government's Tax Plan at Spring Statement. This details the government's commitment to boosting productivity and growth by creating the conditions for the private sector to invest more, train more and innovate more, helping to foster a new culture of enterprise around capital, people and ideas.

The Government should also look to accelerate the UK's transition to a more secure energy supply whilst also reaffirming their commitment to net zero and a just transition. (Paragraph 78)

Although, as the report recognises, Russian imports only account for 8% of the UK's energy, we have committed to phasing out Russian oil and coal by the end of 2022 and Russian liquefied natural gas imports as soon as possible thereafter. We recognise the pressure that has been put on the UK energy markets and the rising prices for consumers. We are focusing on delivering a more independent energy system, bolstering our energy security, reducing our exposure to volatile fossil fuel markets, and moving towards a future in which our energy will come predominantly from low-carbon sources. For example, we have committed to decarbonising the GB electricity system by 2035, subject to security of supply.

Last year we published the Net Zero Strategy, which set a clear vision for how we will transition away from fossil fuels as the primary source of energy towards low-carbon sources. On 7 April 2022, the Government published the British Energy Security Strategy in response to expensive and rising fossil fuel prices, exacerbated by Russia's invasion of Ukraine. The strategy accelerates our transition to secure, clean and affordable British energy for the long term in a series of bold commitments which will put Great Britain at the leading edge of the global energy revolution. Alongside the Net Zero Strategy, it is driving £100 billion of private sector investment into new British industries by 2030, including off-shore wind.

It is important that we recognise that net zero should be a smooth transition, not an immediate extinction, for oil and gas. We will continue to need gas to heat our homes and oil to fill up our tanks for many years to come—so the cleanest and most secure way to do this is to source more of it domestically with a second lease of life for our North Sea.

Our commitment to delivering a fair and just transition to net zero remains paramount. Accelerating the transition from fossil fuels depends critically on how quickly we can roll out new renewable and low carbon capacity. The Net Zero Strategy has already put the UK at the forefront of many renewable technologies, delivering £40 billion of private investment in under two years. The Energy Security Strategy goes further and faster, and demonstrates the Government is serious about delivering a decarbonised electricity system at least cost to consumers whilst maintaining security of supply.