Compliance with the indirect provision ban – implications for financial intermediaries and other economic actors

11.03.2022

Key takeaways

- **The Ordinance on Measures in connection with the Situation in Ukraine prohibits not only the direct but also the indirect transfer of funds or provision of economic resources to Subjects of Sanctions**
- **The assessment of whether there is an indirect provision of resources is challenging**
- **Financial intermediaries holding or managing funds and economic resources which belong to or are controlled by Subjects of Sanctions should implement a compliance regime based on three pillars: modified sanctions list reconciliation, risk-based know-your-customer processes, and flanking contract design**

Introduction

Since 28 February 2022, 6:00 p.m., any financial intermediary holding or managing funds and economic resources which belong to or are controlled by individuals or entities designated in Annex 8 (Subjects of Sanctions) to the Ordinance on Measures in connection with the Situation in Ukraine (Ordinance) has to comply with Article 15 et seq. of the Ordinance. This newsletter shall focus on the prohibition of indirect transfer or provision of funds or economic resources to Subjects of Sanctions according to Article 15 para. 2 in fine of the Ordinance.

Pestalozzi Rechtsanwälte AG
Feldeggstrasse 4
CH-8008 Zürich
T +41 44 217 91 11
zrh@pestalozzilaw.com

Pestalozzi Avocats SA
Cours de Rive 13
CH-1204 Genève
T +41 22 999 96 00
gva@pestalozzilaw.com

pestalozzilaw.com

Scope of the indirect provision ban

In our previous legal update, we outlined that the decision as to whether certain economic resources are owned or controlled by Subjects of Sanctions, and are therefore justifiably blocked, falls within the competence and responsibility of the financial intermediary in question. We further noted that certain difficulties may arise regarding the assessment of control over funds and economic resources. Finally, we established that the determination of indirect provision of funds and economic resources provides for additional challenges.

A statement by the EU Commission from earlier years (a similar specification by Swiss authorities is still pending at the time of publication according to our knowledge) states that a provision of any economic resources to persons or entities owned or controlled by Subjects of Sanctions constitutes an indirect provision within the meaning of the provision ban. Thus, the indirect provision ban applies if a listed person or entity owns more than 50% of the ownership rights or has any other majority interest. This also applies if shareholders can exercise a controlling influence by other means.

Limitations to the indirect provision ban

It cannot be in the interest of the international community of states to interpret the indirect provision ban without limits. The legal uncertainty due to the indeterminacy of the legal concept would result in economic paralysis. However, financial intermediaries and other economic actors must be aware that there can be no concrete criteria for compliance with the indirect provision ban; in sanction law, it is not the manner of provision that matters, but only the objective of the sanction. Economic resources must not end up in the hands of Subjects of Sanctions – otherwise any restrictive measures would be practically ineffective. For financial intermediaries and other economic actors, this means taking a risk-based approach that minimises the risk of a violation through internal due diligence processes on the one hand and good risk and compliance management on the other.

Implications for compliance

Although Swiss sanctions law does not provide for any explicit exemption from liability clauses, the general principles of criminal and administrative fine law apply, resulting in a limitation of liability. Accordingly, financial intermediaries and other economic actors must demonstrate that they can exclude the possibility of a violation through risk-based compliance and control structures. This can be ensured with a compliance regime based on the following three pillars:

Modified sanctions list reconciliation

Financial intermediaries and other economic actors should introduce a modified sanctions list reconciliation that takes into account ownership and control structures. This should be in addition to a direct list reconciliation between business partners and entries on sanctions lists.

Risk-based know-your-customer processes

Companies should ensure processes that enable the best possible knowledge of their business partners in order to exclude negligent violations of domestic and foreign sanction law as far as possible. Risk indicators can be communicated and accessed through appropriate training and checklists.

Flanking contract design

The third element of risk mitigation is to take contractual precautions to exclude violations of the indirect provision ban as far as possible. In this respect, we would recommend a multi-layered approach, addressing not only compliance and end-use clauses but also essential provisions such as subcontracting and distribution channels.

Pestalozzi has set up a team to address the wide range of legal issues companies are facing with regard to sanctions. Visit our Sanctions Resource Center to receive fast, practical and effective advice.

Contributors: Oliver Widmer (Partner), Daniela Fritsch (Senior Associate)

No legal or tax advice

This legal update provides a high-level overview and does not claim to be comprehensive. It does not represent legal or tax advice. If you have any questions relating to this legal update or would like to have advice concerning your particular circumstances, please get in touch with your contact at Pestalozzi Attorneys at Law Ltd. or one of the contact persons mentioned in this Legal Update.

© 2022 Pestalozzi Attorneys at Law Ltd. All rights reserved.

Andrea Huber

Partner
Attorney at law, LL.M.

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 41
andrea.huber@pestalozzilaw.com



Oliver Widmer

Partner
Attorney at law
Head Financial Services

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 42
oliver.widmer@pestalozzilaw.com



Kern Alexander

Of Counsel
Attorney at law, Prof. Dr.

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 54
kern.alexander@pestalozzilaw.com

