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TARGETED ECONOMIC SANCTIONS REGIME FOR FINANCIAL INSTITUTIONS

In the recent years financial institutions have faced tough penalties due to violation of international sanction prohibitions. Especially the United States has been applying such sanction aggressively. The US Office of Foreign Asset Control (OFAC) –tasked with administering and enforcing economic sanctions against targeted foreign countries, regimes, terrorists, international narcotics traffickers, and persons engaged in activities related to the proliferation of weapons of mass destruction, among others- has concluded settlement agreements with a number of financial institutions. The settlement agreement entered into with the French PNB Paribas on 30 June 2014, according to which the bank agreed to a settlement in the amount of almost one billion USD, has sparked off a fierce debate as to whether a state can impose heavy penalties on foreign financial institutions. This raises the broader questions:

- What is the legal framework for international economic sanctions, and where does it emanate from?
- How does the international sanction regime work?
- What are the implications for financial institutions?

The legal basis for imposition of international economic sanctions is Article 41 of the United Nations Charter. Founded as a response to the Second World War, the primary purpose of the UN is to maintain international peace and security. The Security Council is the principal actor charged with carrying out that purpose. It enjoys very broad powers acting under Chapter VII of the UN Charter. The most effective discretion conferred on the Security Council is the use of force under Article 42. However, before invoking such authority in case international peace and security is threatened or breached, the Security Council must apply diplomatic or economic measures under Article 41.

It has been witnessed that the Security Council has applied economic sanctions widely. Several states, such as Iraq, Iran and Cuba, have undergone long-continued

embargoes. However, the rapid change in the world order has caused emergence of new types of threats to international peace and security. In addition to states, the new era sanctions regime included also non-state actors. The Security Council has paid a great deal of attention to fight global terrorism. It passed (the eminent) Resolutions 1267 and 1373 so as to end financial sources of terrorism. The targeted sanctions regime envisaged in these resolutions created certain obligations for states and financial institutions.

The sanctions regime requires states to take positive actions at national and international level. States are under a duty to initiate mutual cooperation. The mode of coordinated actions may appear as an effort at the UN level (i.e. participating in the Security Council blacklisting procedure) or as a multilateral agreement. As an example for the latter, the Financial Action Task Force (FATF) has developed a series of Recommendations so as to combat terrorism financing and money laundering. Although stemming from such an inter-governmental agreement serving a specific purpose or the pertinent Security Council orders, states are to implement their international obligations at national level.

The primary responsibility of states at home is to produce regulations and establish mechanisms in line with the targeted economic sanctions regime. After conducting a risk assessment, countries must apply a risk-based approach in order to mitigate the likely outcomes of such risks. They must designate an authority equipped with the power to coordinate the combat against anti-money laundering, terrorism financing and other causes of targeted sanctions. The coordination must be effective in the areas of asset freezing, confiscation, supervision and law enforcement policies.

Since most of the violations take place through financial transactions, the bulk of state actions/regulations with respect to economic sanctions concerns financial institutions. Hence, the financial world must be prepared for the concomitant consequences of the targeted financial sanctions regime. The onerous responsibility of financial institutions is to carry out customer due diligence and record-keeping. They should also develop a compliance programme to ensure that their transactions such as

credit agreements, insurance policies and corporate acquisition agreements meet the requirements of the national and international targeted sanctions regime. However, when acting as such, financial institutions must be aware of the need for caution that they do not violate the relevant laws, i.e. the secrecy laws. This, in turn, necessitates invoking expert guidance.

As LBF Partners, we offer high-quality legal consultancy on national and international economic sanctions laws. Our service includes a tailor-made impact assessment, due diligence guidance, and training. We also offer a first class consultancy on jurisdictional conflicts stemming from the targeted sanctions process