

Guidance Note – Ensuring food security through the implementation of firewalls in cases of EU entities trading in agricultural and food products and controlled by a designated person or entity

Executive summary

When implementing restrictive measures in view of Russia's actions destabilising the situation in Ukraine, the European Union is committed to avoiding all measures which might lead to food insecurity around the globe¹

The implementation of asset freezing measures adopted in the context of Regulation 269/2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine can be particularly complex in cases where an EU entity is controlled by a designated person or entity, in particular because the asset freeze extends to all assets owned, held or controlled by this non-designated entity.

More specifically, several cases concerning the trade in agricultural and food products, including wheat and fertilisers, have been brought to the Commission's attention in the past months. It is necessary to ensure that those cases may not lead to food insecurity around the globe.

In order to solve those specific cases, the Commission services consider that it is possible to implement 'safeguards' to prevent the designated person from exercising control over the non-designated EU entity. Such a framework (also known as a 'firewall') removes the control by the designated person so that the EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers can continue, while keeping the funds and economic resources owned by the designated person frozen. This document provides guidance to support the implementation and recognition of such firewalls by Member States to solve those specific cases, thereby enhancing their effectiveness and the uniform application of EU restrictive measures.

1. Introduction

1.1 Objectives of this Guidance Note

Over the past year, the EU has adopted an unprecedented set of sanctions targeting those responsible for the brutal aggression of Russia against Ukraine. These sanctions do not target trade in agricultural and food products, including wheat and fertilisers, between third countries and Russia.

¹ For restrictive measures adopted in Council Regulation 833/2014, this has been explicitly stated in Recital 12 of Council Regulation 2022/1269: "The Union is committed to avoiding all measures which might lead to food insecurity around the globe. Consequently, none of the measures in this Regulation or any of those adopted earlier in view of Russia's actions destabilising the situation in Ukraine target in any way the trade in agricultural and food products, including wheat and fertilisers, between third countries and Russia."

To mitigate possible unintended negative effects of these measures on EU operators trading in agricultural and food products, the Commission services consider that it is possible to implement ‘safeguards’ to prevent the designated person from exercising control over EU entities.

Following several cases with significant implications which have been brought to the Commission services’ attention, in the very sensitive and protection-deserving area of trade in food and agricultural products, including wheat and fertilisers, the Commission considers it is appropriate to issue these guidelines.

This document provides guidance concerning the implementation and recognition of firewalls by Member States for EU entities’ business operations in the trade in agricultural and food products, including wheat and fertilisers, thereby enhancing their effectiveness and the uniform application of EU restrictive measures.

1.2 Value of this Guidance Note

The Commission, in its role as a guardian of the EU Treaties, monitors the implementation of Union law by Member States, under the control of the Court of Justice of the European Union. The purpose of this document is to give practical guidance on compliance with EU sanctions while handling cases where an EU entity operating in in the trade in agricultural and food products, including wheat and fertilisers, is controlled by a designated person². It seeks to ensure that EU law is applied consistently across the territory of the Union by setting out criteria relevant for Member States’ national competent authorities (‘NCA’) which are in charge of implementing sanctions.

1.3 ‘Control’ in EU sanctions

EU restrictive measures (‘sanctions’) establish that the freezing of funds and economic resources covers the assets belonging to, owned, held or controlled by those specifically listed in the respective annexes to the EU legal acts. Such a provision typically reads: “[a]ll funds and economic resources belonging to, owned, held or **controlled** by any natural or legal persons, entities or bodies, or natural or legal persons, entities or bodies associated with them, as listed in Annex [X], shall be frozen”³ (emphasis added). EU sanctions also provide that no funds or economic resources can be made available, directly or indirectly, to or for the benefit of a designated person⁴.

This paper addresses situations where a designated person controls a non-designated EU entity operating in the trade in agricultural and food products, including wheat and fertilisers. This paper does not address situations of ownership by a designated person. In this case, divestment by the designated person, when provided for in the Regulation⁵, is the preferred option.

If a designated person refuses to relinquish control over an EU entity operating in the trade in agricultural and food products, including wheat and fertilisers, there is a rebuttable presumption that the control

² This guidance note refers to ‘designated person’ in reference to ‘natural or legal persons, entities or bodies’ for ease of understanding.

³ For instance, Article 2(1) of Council Regulation (EU) No 269/2014 of 17 March 2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine.

⁴ For instance, Article 2(2) of Council Regulation (EU) No 269/2014 of 17 March 2014 concerning restrictive measures in respect of actions undermining or threatening the territorial integrity, sovereignty and independence of Ukraine.

⁵ For example, Article 6b(3) of Council Regulation (EU) 269/2014 enables national competent authority to allow the operations necessary for designated owners to divest from their EU companies, thereby removing ownership.

extends to all assets owned by the latter. Such assets must be frozen. Otherwise, designated persons could circumvent the asset freeze imposed on them by continuing to have access to funds or economic resources through the non-designated third parties that they control⁶. In a similar vein, the making available of funds or economic resources to a non-designated entity, which are controlled by a designated person, amounts to making them indirectly available to the latter.

In order to mitigate certain undesired effects, EU regulation 269/2014 provide for certain limited exceptions from the asset freeze and prohibition to make funds or economic resources available to such entities. In spite of these legal exceptions (derogations), in practice it has proved very complex for EU entities operating in the trade in agricultural and food products, including wheat and fertilisers, and controlled by designated persons to continue operating after the designation of the latter. Existing derogations typically do not cover all possible transactions that such an EU entity may need to carry out in the trade in agricultural and foods products, including food and fertilisers. The scope of such derogations cannot be expanded without rendering the asset freeze on the designated person ineffective. In addition, the long-term freezing of a non-designated entity's assets can have drastic negative consequences for the entity, all the way to possible bankruptcy. Accordingly, the Commission's services support the implementation of firewalls for EU entities operating in the trade in agricultural and food products, including wheat and fertilisers.

1.4 Objectives of a firewall

The business operations in the trade in agricultural and food products, including wheat and fertilisers, of an EU entity controlled by designated persons may have significant importance for the EU economy and world market. Furthermore, such entities may belong to the same group and be present (e.g. through subsidiaries) in several EU Member States or third countries imposing similar sanctions.

In some limited cases, the designation of an individual found to exercise control over EU-based companies operating in the Russian fertiliser sector has disrupted the business operations of these EU entities. While this has not prevented the designated persons from using their product lines in Russia, the possible negative impact that this situation may (be perceived to) have on food security in third countries should be avoided and mitigated as far as possible. Therefore, the Commission supports the implementation of safeguards (firewalls) to prevent the designated person from exercising control over the entity.

A firewall brings about a structural change in an entity's corporate governance to remove the designated person from the day-to-day operations and any business decisions of the entity and the resulting resources and profits. It ring-fences the entity's assets and forestalls the making available of any economic resources to the controlling designated person. By doing so, a firewall enables an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers to operate, under strict conditions, unimpeded by the control of a designated person or entity. This means that the EU entity operating in the trade in agricultural and food products, including wheat and fertilisers, and operating under a firewall can have access to funds and economic resources, including the provision of services. The firewall ensures that no such funds or economic resources are made directly or indirectly available to

⁶ See Commission opinion of 19.6.2020 on Article 2 of Council Regulation (EU) No 269/2014.

that person. Irrespective of the firewall, the funds and economic resources of the designated person remain frozen.

Accordingly, a robust firewall put in place for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers means this entity can continue operating and avoiding potential negative consequences on the accessibility of food and fertilisers in third countries at risk of food insecurity. The EU is committed to address the challenges to global food security exacerbated by Russia's war against Ukraine and the implementation of firewalls in the agricultural and food sector participates to the realisation of this objective.

This document is part of the extensive guidance that the Commission has provided to Member States national competent authorities, to address situations relating to the agricultural and food trade. The following sections provide guidance on the possible layout of a firewall. They aim to specify the conditions under which this framework should be implemented and recognised, in order to ensure its effectiveness and a homogeneous implementation by the Member States.

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1. Practical implementation of a firewall

2.1 Requirements for a firewall

a) Entities for which a firewall may be established

The implementation of a firewall should take into account the positioning and significance of the EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers on a national market or the European market, both in terms of market positioning and employment volume.

The establishment of a firewall is the preferred option for EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, as it aims to protect the interests of entities present on the European market—and the accessibility of agricultural and food products to third countries dependent on Russia supplies which cannot obtain those other than via the involvement of an EU entity controlled by a designated person. The relevance of focusing firewalls on EU-based entities is further reinforced by the interventions that may be necessary on the management of the entity (see section 2.2).

b) The removal of the designated person

The firewall should be constructed as a mechanism that ensures that the designated person is not involved in day-to-day and business decisions of the EU entity and that no resources from the entity will be accrued directly or indirectly. The designated person should not have the possibility to assert influence over the conduct of the EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers. It should be ensured that the designated person does not engage in any executive activities like those of a director, nor assume any decision-making role.

The designated person controlling a company may own shares. As indicated above, this document only addresses control by a designated person and not ownership, yet there may be cases of minority shareholding. In any case, designated shareholders cannot exercise their voting rights in a company nor benefit from any economic resources, whether directly or indirectly, under any circumstance or for any purpose. Restructuring of ownership (i.e. the sale of shares by a designated person) is also prohibited by

virtue of the asset freeze. Such a sale can only be done if the relevant EU Regulation contains a derogation to this end and the NCA grants an authorisation. The proceeds of the sale must be frozen.

2.2 The implementation of a firewall

a) Firewalls by legislation

A Member State may set up a firewall by intervening directly on the governance of the ‘decoupled’ entity through legislation. The structure of a firewall by legislation will differ from country to country given the diversity of legal systems in the EU. Several areas of law, such as insolvency or competition law, may provide inspiration for such a framework.

The legislation must grant the NCA the ability to appoint a third party such as a temporary administrator or supervisor. This third party must act independently and report directly to the NCA. The third party must be suitable, with good repute and sufficient experience to fulfil its duties.

The third party would take actions necessary to ensure the proper implementation of EU sanctions, and provide the NCA with regular accounts regarding the creation and operation of the firewall. The third party would furthermore ensure that transactions carried out by the entity are not directly or indirectly benefitting the designated person.

To ensure the independence of the temporary administrator or supervisor, the NCAs may refer to the criteria outlined in the Annex.

If a Member State lacks the legislative toolset to implement such a firewall, it may consider adopting or amending legislation.

b) Firewalls by operators

The establishment of a firewall by an operator refers to the case where an entity decides to implement safeguards to decouple itself from a designated person which controls it. This initiative aims to remove the presumption of control and to avoid the underlying risks, notably financial and credit institutions’ refusal to carry out transactions in connection with this entity, or to avoid a functioning that would rely on the authorisations granted by the NCAs on the basis of existing derogations. However, to be effective, the resulting changes in governance practices, as decided directly by the operator, must comply with the strict conditions that a firewall requires, particularly in terms of independence. Ultimately, the firewall must remove the control of the designated person, as explained in section 2.2.

To ensure that the safeguards established by the entity effectively rule out any presumption of control by the designated person, operators are encouraged to rely on an external audit, acting in full independence. The external audit process should be based on particular information provided by the entity, including its articles of association, bylaws, shareholder structure, as well as a description of the changes that have taken place that would allow for the removal of control by the designated person (e.g. notably board minutes attesting to management changes in the entity).

The external auditor should also have direct access to the entity’s executives (directors) in order to be able to testify that the entity’s operations are not subject to the influence of the designated person.

Finally, it is expected that the chief executive of the entity will give written undertakings, referring to its responsibility on the established firewall. If deemed relevant, a firewall established by the operator could entail the intervention of a third party exercising a similar role as described for a firewall by legislation⁷.

The audit must determine that the designated person is neither in a position to exercise influence nor can in any way benefit from the assets of the entity (e.g. dividends, loan arrangements etc.).

If a firewall is not effectively established, the presumption is not rebutted and the NCA must keep the entity's assets frozen. In addition, in the event of non-compliance with the firewall commitments, the entity and the relevant individuals must be held accountable according to Member State penalties applicable to infringements of the provisions of the relevant EU Regulation.

c) Exchange of information regarding cross-border situations

Designated persons can be involved in entities located in multiple Member States. For instance, a designated person can exercise control over several EU subsidiaries or a controlled entity may own several EU subsidiaries. It may be the case that one such entity is located in a non-EU country implementing similar measures. Accordingly, the implementation of a firewall may be necessary in several jurisdictions.

Where a cross-border situation appears, Member States should immediately reach out to other relevant Member States to engage collectively on the situation. Such exchanges could facilitate a shared assessment of control over the respective subsidiaries and discuss the possible need for firewalls. The Commission can facilitate the exchange of information for specific cases. The implementation of firewalls in only certain Member States may disturb the activities of the other related entities or the group as a whole, for instance if one such entity is an essential provider of internal services. This is detrimental to the uniform application of EU sanctions and runs counter the objectives supported by these safeguards.

For the sake of clarity and to avoid adverse effects, the NCA where the 'controlled' entity is incorporated should be the one in charge of creating and/or monitoring the implementation of the firewall. Once implemented, in all cases firewalls should be recognised – provided that they are established according to the criteria that are set in this guidance, in order to work effectively, as discussed in the following section (section 3).

2. Recognition of firewalls

As discussed above, the establishment of an adequate firewall should 'decouple' the controlled entity from the designated person. In practice, once a firewall is in place, the frozen assets of the EU entity operating in the trade in agricultural and food products, including wheat and fertilisers, can be released and economic resources can be provided to the 'decoupled' entity. The previously controlled entity may resume its business operations. Yet, a firewall will only be operational where other operators engage with the decoupled entity. Recognition guarantees that a firewall which is set up in one Member State can produce effects in other Member States, ensuring its effectivity.

Where a firewall by legislation and/or voluntary changes to corporate governance by an operator comply with the letter and spirit of this guidance document, the pre-requisite for recognition should be satisfied.

⁷ See section 2.2 (a) and the Annex.

3.1 Implementation of recognition by Member States

a) Firewall by legislation

The criteria set out in the Annex guide the appointment and role of a third party appointed in the context of firewalls for EU entities operating in the trade in agricultural and food products, including wheat and fertilisers, set up via legislation. In doing so, the criteria seek to bridge differences in national frameworks to facilitate mutual recognition of firewalls for EU entities y's business operations in the trade in agricultural and food products, including wheat and fertilisers, and support uniform implementation of EU sanctions.

Where the criteria for recognition of such a firewall are met, other Member States are invited to recognise such a framework. Member States are encouraged to publish translations of their legislation to facilitate this process.

Operators may be reluctant to recognise a firewall for EU entities' business operations in the trade in agricultural and food products, including wheat and fertilisers, by legislation implemented in a Member State other than their place of business. Member States should support such recognition. When requested or at its own initiative, a Member State that has implemented a firewall by legislation should present its framework and share relevant information with other Member States. Member States should be in a position to satisfy themselves that the measures put in place indeed constitute an effective firewall. The Commission welcomes technical discussions in its Expert Group on EU sanctions.

Member States may choose to conclude a technical agreement for recognition of the firewall for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, which would be shared amongst all Member States and the Commission. The Commission would facilitate such agreements. This document could be published and relied upon by operators.

A Member State's refusal to recognise a firewall for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, can be justified where the framework set up by a legislator does not meet the letter or spirit of the criteria in this guidance, or if there is insufficient information about the framework upon request.

b) Firewall by operators

As set out in section 2.2 (b), an operator that sets up a firewall for an EU entity operating in the trade in agricultural and food products, including wheat and fertilisers may resort to an external third party, such as an auditor, to implement and/or certify the effectiveness of the changes to the entity's corporate governance.

In addition, a Member State may also organise an authentication process by which it would recognise the removal of control. In this case, an NCA must carry out the necessary checks to guarantee that the letter and spirit of this guidance have been respected. The NCA should also receive assurance that the designated person is no longer involved in the entity, for example by written statements from senior management.

A Member State may condition the authentication of a firewall for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, upon the conduct of an external audit. In this case, the NCA should have the possibility to engage directly with the auditor to

carry out its authentication and access all audit and corporate documents. The NCA may amend the scope of the audit as appropriate and reserve its right to refuse recognition where the auditor was not suitable or competent to perform such a mission.

Once the compliance of the firewall for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, is established, the NCA should issue an official written confirmation. This document can be circulated by the entity as necessary to other Member States or any relevant party (e.g. banks, clients, etc.). Such an authentication should be recognised by other Member States similarly to firewalls by legislation.

Where an operator does not resort to an external audit, it may publish a declaration of removal in which it details the changes implemented to remove control by the designated person. It is the responsibility of its business partners to assess that such changes are in compliance with EU sanctions and to carry out the necessary due diligence checks.

3.2 Recognition of firewalls in cross-border situations

Where a cross-border situation appears (see section 2.2 (c)), and whereas a firewall for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, has been established in one or more subsidiaries of the same group, Member States must immediately reach out to other relevant Member States to share information to demonstrate the effectiveness of the firewall. To this end, Member States should rely on the 'technical agreement' obtained in the framework of a firewall by legislation (see section 2.2 (a)) and on the 'written undertakings' issued by the entity in the framework of a firewall by operator (see section 2.2 (b)).

While it is up to the competent national authorities to determine the recognition of firewalls for an EU entity's business operations in the trade in agricultural and food products, including wheat and fertilisers, under the circumstances as they deem appropriate, their mutual recognition will be facilitated, provided that they are established according to the criteria specified in this guidance.

Annex: Criteria for the appointment of a third party in implementing a firewall by legislation

Regarding the administration or supervision:

- Surveillance and oversight (e.g. via an appointed administrator or supervisor) by an independent third party:
- General reporting obligations of the third party or board of directors to the NCA (e.g. on the nature of contacts between entity and the designated person, evidence to demonstrate that the firewall is implemented and subsequently respected).
- Where applicable, the administrator/supervisor may replace the designated person in the execution of the following rights:
 - o attending meetings of the general meeting of shareholders, associates, board of directors, or any other meeting on the management of the entity;
 - o accessing locations of operation of the entity;
 - o accessing documents received by or emanating from the entity, related to financial-accounting, legal or otherwise;
 - o remuneration for activities carried out.
- The administrator or supervisor must take actions necessary to ensure the proper implementation of EU sanctions and that transactions carried out by the entity are not directly or indirect benefitting the designated person.
- The administration or supervision is a temporary measure. It may last for as long as the relevant EU restrictive measure is in place. EU sanctions are kept under regular review to ensure that they continue to contribute towards achieving their stated objectives.

Regarding the administrator or supervisor:

- The administrator or supervisor is either a natural or a legal person (e.g. an accounting company).
- The decisive requirement is the independence of the administrator or supervisor.
- The administrator or supervisor must provide guarantees in terms of honourability, experience and competence to carry out the functions entrusted to it. To assess and monitor the administration and supervision, the supervisor or administrator should have regular direct reporting obligations to the NCA.
- The administrator or supervisor should be compensated by the administered/supervised entity.
- The liabilities of the administrator or supervisor are subject to national provisions. It may be held responsible for a violation of EU sanctions, for instance by assisting the circumvention of these measures.

Regarding procedures for the appointment of the administrator or supervisor:

- An application for the appointment of an independent administrator or supervisor may be made by the entity to the NCA of a Member State.
- Alternatively, an external administrator or supervisor may be installed by the entity itself with a notification made to the NCA for verification.