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Review article

ECONOMIC SANCTIONS BASED ON INTERNATIONAL AND EU LAW

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ABSTRACT

The use of "sanctions" is an instrument of the Common Foreign and Security Policy for the EU, which aims to prevent and respond to various crises. The term "sanctions" covers a range of measures, particularly arms embargoes, travel restrictions, asset freezes and other economic restrictions. The EU currently applies several sanctions packages, some of which are part of a range of sanctions based on international law and others which go beyond it.

The economic effects of the restrictions also affect civil law relations. Their scope is not limited to the actors on the sanctions list but extends to persons directly and indirectly associated with them, ultimately affecting the legal relations of persons not on the sanctions list who have no economic links with the sanctioned country or region.

In the first part, the study provides an overview of the system of "sanctions policy", the reasons for and the means of applying restrictive measures, including an introduction to the powers and case law of the Court of Justice of the European Union concerning sanctions. The second part of the study deals with economic sanctions. Firstly, it identifies the scope of restrictive measures as economic restrictions. Secondly, it describes the civil law implications of economic sanctions from the courts' perspective when applying the law by describing the applicable legal provisions. On the other hand, the case law of the Court of Justice of the European Union will be presented to show the obligations imposed by the EU on the courts applying economic restrictions in the conclusion and performance of specific legal transactions and in resolving disputes arising from them.

The study is not concerned with assessing the necessity and effectiveness of sanctions but only with their effects as legal facts on the application of the law.

***Keywords**: common commercial policy, economic sanctions, EU law, principle of effectiveness*

1. SANCTIONS POLICY, IN BRIEF

At times, a word may possess contradictory meanings; such is the case with *'sanction,'* which can denote both 'to permit, encourage' and 'to punish to deter'. From the beginning, two fundamental notions of law were wrapped up in this word: law as something that permits or approves and law that forbids by punishing.[1] In this paper, we use the term sanction in the latter sense. One more linguistic remark: in the plural, sanctions mean a coercive measure, especially one taken by one or more states against another guilty of violating international law.

As restrictive measures are applied by states, sanctions are derived from sovereignty and are allowed by international law to settle disputes between states. Part of sovereignty is the power to decide whom a state allows to enter or transit its territory and determine who can trade on its territory and with what; these are the arms embargoes and travel restrictions. A sovereign can restrict property disposal on its territory and the business activities of its citizens and legal entities in other states; these are asset freezes and other economic restrictions. Restrictions may be lawful, under the rule of law, or contrary to the rule of law, arbitrary. Sanctions are based on a variety of grounds, typically the preservation of international peace and security or to achieve a foreign policy goal, in particular, the protection of human rights, the fight against terrorism, chemical disarmament, weapons of mass destruction, the fight against cyber warfare, the fight against corruption. Their effectiveness is enhanced if they are enforced with the same content by a group of states, like the United Nations (UN) or the European Union (EU)[2]. The sanctions based on international and EU law are presented below.

1.1. Types of Sanctions

As regards the subject of sanctions, a distinction can be made between classical and horizontal sanctions. Classical sanctions are imposed on individual states or territories. Horizontal or smart or targeted sanctions are imposed on specific persons or bodies. Classical sanctions have been sanctions on countries, but they have resulted in significant humanitarian damage, and it is questionable how effective they have been in achieving the desired effect. Increasingly, 'individual' sanctions have been used, first in the areas of terrorism, cyber-attacks, and chemical weapons-related measures. The advantage of horizontal sanctions is that they are personalised and can, therefore, be used effectively against organisations independent

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1 American Heritage Dictionary of the English Language, Fifth Edition. *S.v.* , *sanction* [https://www.thefreedictionary.com/sanction], Accessed: 05 April 2024 .

2 van Bergeijk, P.; Biersteker, T., *How and When Do Sanctions Work? the Evidence. On Target? EU Sanctions as Security Policy Tools*, [doi:10.2815/710375]. Accessed 05 April 2024.

of national borders, e.g. terrorist organisations.[3] They are also flexible enough to allow certain responsible persons or bodies to be added to the sanctions list while allowing for the possibility of deletion.

Sanctions are tools for achieving foreign policy goals; the subject matter of sanctions depends on the objectives and legal possibilities of the state or entity applying them. Using the example of the UN, the relation of the objective and possibilities are as follows: The UN Security Council can take action to maintain or restore international peace and security under Chapter VII of the United Nations Charter. The Security Council may decide what measures not involving the use of armed force are to be employed to give effect to its decisions, and it may call upon the Members of the United Nations to apply such measures. These may include complete or partial interruption of economic relations and rail, sea, air, postal, telegraphic, radio, and other means of communication and the severance of diplomatic relations.[4] The UN has a broad mandate, but its means to do so are limited. In the next chapter, the EU will be used as an example to illustrate in detail how UN sanctions influence and facilitate other sanctions policies. Before doing so, however, it is necessary to examine how the protection of human rights has been included among the subjects to be protected by sanctions.

The idea of horizontal sanctions in the field of human rights protection is relatively new, originating in the United States. In response to Sergei Magnitsky's death and to address human rights violations and corruption, the US passed the "Magnitsky Act" in 2012, which targeted Russian officials believed to be involved in Magnitsky's detention, abuse and death by freezing their assets and banning their entry to the United States. The Global Magnitsky Act, adopted in 2016, has gone beyond the scope of one controversial incident. The Magnitsky Act has been expanded and applied to other countries, which allows the US government to sanction individuals from any country involved in severe human rights abuses or significant corruption.[5] The Global Magnitsky Act is a global response to substantial human rights and corruption violations.

Several other countries, including the United Kingdom, Canada, and the European Union, have also adopted their versions of Magnitsky-like sanctions legislation to hold individuals accountable for human rights violations and corruption world-

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3 European Union Institute for Security Studies, Portela, C., *A blacklist is (almost) born – Building a resilient EU human rights sanctions regime*, [https://data.europa.eu/doi/10.2815/408461], Accessed 05 April 2024.

4 Article 41 of the United Nations Charter.

5 Congressional Research Service, *The Global Magnitsky Human Rights Accountability Act,* 2020, [https://crsreports.congress.gov/product/pdf/IF/IF10576] Accessed 05 April 2024

wide. In December 2020, the EU adopted the Council-Adopted Decision (CFSP) 2020/1999 and Council Regulation (EU) 2020/1998, establishing a framework for targeted restrictive measures to address serious human rights violations and abuses worldwide. On this basis, the EU's Member States should lay down rules on penalties applicable to infringements of this Regulation's provisions and ensure that they are implemented; this has resulted in a mosaic of practices across the EU, involving more than 160 designated competent authorities within Member States.[6]

1.2. Development of EU's Sanctions Regime, in Brief

1.2.1. Development of EU's Sanctions Regime

Sovereignty is the basis for the application of sanctions. Still, a group of states sometimes realises it is in their state's interest to exercise sovereignty jointly with other states on specific issues. Along these lines, the EU Member States have agreed to "establish among themselves a European Union, (…) on which the Member States confer competences to attain objectives they have in common."[7]. One of the competences exclusively delegated to the EU is the common commercial policy.[8], which is an area inevitably affected by applying economic restrictive measures. As a consequence, sanctions applicable by EU Member States must also take into account a specific legal context, the rules of EU law, and therefore, these provisions have inevitably appeared in EU law and have evolved over the past decades in parallel with the development of the Community and the sanctioning regimes.[9]

The EU sanctions policy can be divided into three periods[10], which are also seen as a developmental arc. As will be seen, this evolution has concerned partly the nature and targeting of sanctions and partly the rules for adopting these measures.

In the early period up to the Maastricht Treaty, the question of the sovereignty of the Member States in the application and enforcement of sanctions was not raised

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6 European Parliament, Directorate-General for External Policies of the Union, Portela, C., Olsen, K., *Implementation and monitoring of the EU sanctions' regimes, including recommendations to reinforce the EU's capacities to implement and monitor sanctions*, [https://data.europa.eu/doi/10.2861/747624], Accessed 05 April 2024.

7 Article 1 TEU (Lisbon).

8 Article 3 (1) e) TFEU (Lisbon).

9 van Bergeijk, P.; Biersteker, T., *How and When Do Sanctions Work? the Evidence. On Target? EU Sanctions as Security Policy Tools*, Accessed 05 April 2024.

10 Viktor S., *Korlátozott tagállami mozgástér a közös kül- és biztonságpolitikában? – a (gazdasági) szankciók alkalmazásának jogi feltételei az Európai Unióban*, (Limited room for manoeuvre for Member States in the Common Foreign and Security Policy? - the legal conditions for the application of (economic) sanctions in the European Union) Állam- és Jogtudomány, Vol. LIX, No. 2, 2018, pp. 53 – 71.

between the Member States and the Community institutions. UNSC sanctions were transposed into the legal systems of the Member States independently and at different times. The independent implementation by Member States has also led to differences in substance.

By the 1980s, Community interpretation of the law began to suggest that sanctions measures should be adopted within the framework of a common commercial policy due to their trade policy nature. This view was based partly on the need for effective sanctions enforcement by the Community and partly on a new understanding of the division of powers in relation to trade policy.

Az effectiveness, from a legal point of view, implies that the national rules of procedure may not make it virtually or in practice impossible or excessively difficult to exercise rights under EU law.[11] The European Commission, as the guardian of the EU treaties, has the task of enforcing EU law, by monitoring the application of EU primary and secondary law and ensuring its uniform application throughout the EU.[12]

The new understanding of the division of powers concerning trade policy was materialized in Opinion 1/78 of the Court of Justice of the EU. Its relevant element for our topic is that the EU's common commercial policy must extend beyond traditional trade instruments to remain effective. This policy includes measures with non-commercial objectives, such as development, foreign and security policy, and environmental or health protection, as long as they directly impact trade. Article 207(1) TFEU acknowledges this interaction. From 1982 to 1993, before the Maastricht Treaty, trade policy sanctions required unanimous decisions by Member States within the European Political Cooperation framework.[13]

The new legal basis established by the Maastricht Treaty[14] is a regulation in line with the practice of the previous period. These rules and sanctions were decided on a new, two-stage legal basis, based on Article 228a of the Treaty on European Union**.** It made it clear that trade policy measures required based on intergovernmental agreements between Member States would be formulated and implemented uniformly through the powers conferred on the Union. The provision concerned measures against third countries, so it established competence for traditional sanctions against countries but was unsuitable for application to horizontal sanctions.[15]

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11 Case C-49/14 Finanmadrid, [2016] ECLI:EU:C:2016:98 point 40.

12 Article 17 TEU (Lisbon).

13 Opinion of advocate general Sharpston in Opinion procedure 2/15 par 101. [ECLI: EU: C:2016:992].

14 TEU (Maastricht).

15 Meissner K., *How to sanction international wrongdoing? The design of EU restrictive measures,* Rev Int Organ. 2023, pp 61-85.

The Treaty of Lisbon has clarified the legal basis for the imposition of sanctions and, in addition to providing for the application of horizontal sanctions, allows countries to impose "restrictive measures against natural or legal persons and groups or non-State entities."[16].

The sanctions applied by the EU can be divided into three categories.[17]

Firstly, sanctions for the implementation of sanctions adopted by the UN Security Council (hereinafter: UNSC). All EU Member States are also UN Member States, UNSC resolutions are binding on all Member States. If the implementation of a UNSC resolution concerns a shared or exclusive competence of EU Member States, the EU has a legislative obligation. e.g. Afghanistan, Central African Republic. The UNSC's competence is limited to the maintenance of international peace and security, but it has no power to take decisions or restrictive measures on matters other than those covered by the UNSC resolution; therefore, the second group includes sanctions, which are based on a UNSC resolution but which the EU wishes to apply more broadly or more strictly than the UNSC resolution. e.g. Iran and Libya. The third group of cases includes EU autonomous sanctions, which are taken by EU Member States on their initiative in the absence of a UNSC Resolution and are presented as a coherent EU foreign policy. They are not created independently but typically in cooperation with the US or other countries and international organisations. e.g. Libya.

1.2.2. Relevant Case Law - Joint Cases *Yusuf and Kadi vs Council of the European Union*

As we have seen, the Maastricht system of sanctions policy was unsuitable for application to horizontal sanctions. The UN targeted financial sanctions regime was first established by Resolution UNSCR 1267 (1999), in which the United Nations Security Council imposes several measures against individuals and entities associated with Al-Qaida. The EU regulation implementing the first horizontal sanction also raised questions of competence and fundamental rights, which the CJEU interpreted in the Kadi and Yusuf cases and on a criticized dualist approach led to the annulment of the Regulation on fundamental rights grounds.[18]

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16 Article 215 (2) TFEU (Lisbon).

17 Biersteker T.; Portela, C, *EU Sanctions in Context: Three Types*, European Union Institute for Security Studies (EUISS), [http://www.jstor.org/stable/resrep06822], Accessed 05 April 2024.

18 Kokott, J.; Sobotta, C., *The Kadi Case – Constitutional Core Values and International Law – Finding the Balance?,* European Journal of International Law, Volume 23, Issue 4, November 2012, p. 1015–1024.

On 15 October 1999, the UN Security Council adopted Resolution 1267 (1999) ordering, among other things, Member States to freeze funds and other financial resources derived from assets owned or controlled, directly or indirectly, by the Taliban or by any undertaking owned or controlled by the Taliban. The Sanctions Committee designated Yassin Abdullah Kadi and the Al Barakaat International Foundation, based in Sweden, as having links to Usama bin Laden, the Al-Qaida network and the Taliban.

The Council of the European Community has adopted a Regulation freezing the funds and other financial resources of the persons and entities whose names appear on the list annexed to that Regulation. This follows changes to the list drawn up by the Sanctions Committee, which thus included Mr Kadi and Al Barakaat on 19 October 2001.

YA Kadi and Al Barakaat brought actions before the Court of First Instance to annul that EC regulation, claiming that the Council did not have the power to adopt it and that it infringed on a number of their fundamental rights, including the right to property and the right to defence.

The Court of First Instance dismissed the action and maintained the Regulation in force. The Court ruled that, as a general rule, the Community courts have no jurisdiction to review the validity of the Regulation in question and that a Member State's obligation under an international treaty takes precedence over Community law.

YA Kadi and Al Barakaat appealed against these judgments before the Court of Justice.

The Court of Justice set aside the judgment of the Court of First Instance and annulled the EC Council Regulation in so far as it concerns Mr Kadi and the Al Barakaat International Foundation, with effect from the expiry of a three-month period of grace.

Regarding jurisdiction, the Court of Justice confirmed that the Council had jurisdiction to adopt the Regulation based on Articles 60 EC and 301 EC, read in conjunction with Article 308 EC and that the Court of First Instance had erred in law in this respect but had reached the correct conclusion. The review by the Court of Justice of the validity of Community acts concerning fundamental rights must be regarded as an expression in the Community of the constitutional guarantee deriving from the EC Treaty as a separate legal system, which cannot be affected by an international agreement. It pointed out that the subject of the review is the Community Act implementing the international agreement and not the international agreement.

As regards the legal basis for the application of sanctions against persons, it pointed out that the Union and the Community are two integrated but distinct legal systems. The bridge between the Treaties could not be extended to other provisions of the EC Treaty because this would be against the will of the authors of the Treaties. It also pointed out that Article 301 of the EC Treaty could not be used by itself to impose sanctions on individuals. However, it stated that "In as much as they provide for Community powers to impose restrictive measures of an economic nature to implement actions decided on under the CFSP, Articles 60 EC and 301 EC are the expression of an implicit underlying objective, namely, that of making it possible to adopt such measures through the efficient use of a Community instrument".[19] (226)

As regards the right to property and the rights of the defence, it found that the EC Regulation under examination did not provide for a procedure for the communication of the facts justifying the listing of the names of the persons concerned at the same time as or after such listing and that the Council had not informed YA Kadi and Al Barakaat of the facts adopted against them which would have justified their initial listing. That breach of the rights of the defence of Mr Y.A. Kadi and Mr Al Barakaat also amounts to the violation of their right to a judicial remedy, as they could not defend their rights in appropriate conditions before the Community judicature.

The Court also held that freezing the funds constituted an unjustified restriction on Mr Kadi's right to property. The Court considers that the restrictive measures imposed by the Regulation constitute a restriction on that right, which is, in principle, justified. Still, in the present case, the Regulation was adopted without Mr Kadi being afforded any guarantee enabling him to challenge the infringement of his property rights.

2. ECONOMIC SANCTIONS

The preceding sections presented an overview of the foundations of sanctions policy, including its international and EU legal basis and the development of EU law in terms of both the division of powers and the legal basis for the applicability of different types of sanctions. The following section will introduce the general concept of economic sanctions and their relevance in civil proceedings.

2.1. Interpretation of Economic Sanctions under National Law

Sanctions policy is the set of objectives and legal bases for sanctions. As we have seen in the previous examples, individual sanction measures are autonomous legal

[19] Joined Cases C-402/05 P and C-415/05 P, [2008] ECLI:EU:C:2008:461, point: 226.

provisions that respond to specific situations. Such legal provisions are, for example, a UN Security Council Resolution in the case of the UN, a Common Position in the framework of the CFSP and an EU Regulation in the case of the EU. EU sanctions are, in fact, implemented by individual Member States. Although regulation has general application, it is binding in its entirety and is directly applicable in all Member States.[20], it also creates a legislative obligation for Member States to ensure effective enforcement of the EU law[21], e.g. by creating a framework legislation. Ensuring effective enforcement through framework legislation will relieve Member States of needing further legislation if new sanctions are adopted.[22] The advantage of national framework legislation for this paper is that the national legislator determined to use a general definition to ensure that the various economic sanctions are enforced, thus serving as a basis for a definition, which I will illustrate below using the Hungarian example.

The Hungarian State ensures the proper implementation of the financial and property restrictive measures imposed by the EU and the UNSC through the procedural rules contained in Act LII of 2017. The Act lays down general rules for the enforcement of economic sanctions. In this context, the Act defines the concept of economic sanctions in terms of its scope, specifies the persons subject to the restriction in terms of its subject matter, and establishes the organisational framework and procedures for enforcement.

According to the Act's generalised definition, a financial and property restrictive measure is a freezing of funds and economic resources ordered by an EU act or a UNSCR, a prohibition on making funds or economic resources available as provided for in an EU act or a UNSCR, a ban or restriction on financial transactions (transfer of funds) and the related authorisation procedure in cases specified in an EU act or a UNSCR.[23]

It defines by way of reference the subjects of a financial and property restrictive measure as a natural or legal person, entity without legal personality, or a natural or legal person, entity without legal personality, which is subject to an EU act or a UNSCR imposing a financial and property restrictive measure, or a natural or le-

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20 Article 288 TFEU (Lisbon).

21 Muzsalyi R., *Az EU-jog hatása a polgári eljárásjogra.* 2020, Budapest: Akadémiai Kiadó, [https://mersz.hu/hivatkozas/m768aejha_51_p1/#m768aejha_51_p1/], Accessed 05 April 2024.

22 Bismuth, R., *The New Frontiers of European Sanctions and the Grey Areas of International Law,* [https://geopolitique.eu/en/articles/the-new-frontiers-of-european-sanctions-and-the-grey-areas-of-international-law/], Accessed 05 April, 2024.

23 2. § point 5 of Act LII of 2017. on implementing the financial and property restrictive measures imposed by the European Union and the United Nations Security Council.

gal person, entity without legal personality, which is a member of an entity subject to an EU act or a UNSCR imposing a financial and property restrictive measure.[24]

The Act also directly defines the tasks of law enforcement bodies, such as service providers, supervisory bodies, asset registries, and the procedure for appeals. However, as can be seen from the case law below, sanctions and these rules are also applied indirectly, e.g. in the settlement of claims for damages.

2.2. Role of National Bodies

Under the Act, there are three types of national bodies: the supervisory body, the responsible authority, and the courts.

The supervisory body shall ensure that service providers comply with the obligations laid down by law and shall provide information to them.[25]

The authority is responsible for enforcing the rules of the different sanctioning regimes by monitoring economic operators and transactions. In the case of a person or transaction subject to a sanction, it decides on the obligation to refuse a transaction or, if other restrictions are necessary, initiates legal proceedings.[26]

The national court, a key player in the enforcement of sanctions, extends its jurisdiction beyond the restrictions on individual transactions. In civil matters, it undertakes two types of tasks: firstly, the enforcement of the restriction or discharge and, secondly, the remedy of the persons concerned in their application for a remedy regarding enforcement. This comprehensive role of the national court ensures a fair and just enforcement process.

Suppose a person subject to a financial and property restraint measure holds assets subject to a financial and property restraint measure subject to a freezing order in the territory of Hungary. In that case, the service provider obliged to do so may not execute the financial disposition, and the body keeping the property register may not perform the entry, which would result in a change of the right of disposal. The company registry court shall suspend the operation of the company concerned. The regional court having jurisdiction over the location of the assets shall order the assets to be frozen.[27] Suppose the EU act or UN Security Council resolution imposing the sanctioning measure allows for an exemption from asset freez-

[24] 2. § point 6 of Act LII of 2017.

[25] 3. § section 2 and 5 of Act LII of 2017.

[26] 4. § and 5. § of Act LII of 2017.

[27] 5. § of Act LII of 2017.

ing. In that case, the court will decide on a request to lift the freeze concerning the person or item of property concerned by the exemption. The court shall determine the decision based on the conditions and criteria in the EU Act or UNSCR. The discharge decision will be communicated to the other Member States and institutions of the European Union through the Minister for Justice by EU acts.[28]

The above measures taken to enforce a sanction are subject to appeal under the rules of the national implementing law governing the blocking. The appeal may be successful if it is established that the person concerned is not the subject of a financial and property restrictive measure imposed by an EU act or a UNSCR.[29]

2.3. Relevant National Case Law on the National Enforcement of Sanctions

The following simple example illustrates the national court's powers in enforcement and discharge and remedy procedures.

The EU sanction based on which the legal action is brought is to freeze all funds and economic resources belonging to, owned, held or controlled by the natural or legal persons, entities or bodies listed in the Annex to the EU Regulation or by any natural or legal person, entity or body associated with them.

The national authority responsible for enforcing sanctions has detected that a domestic financial institution is directly majority-owned by a company established in another EU Member State whose majority owner is on the EU sanctions list. Based on the sanctioning provision described above, as it is controlled by the legal entity on the sanctions list, the domestic financial institution indirectly became subject to the financial and property restriction measure. The national authority responsible for enforcing the sanctions has initiated a freezing order on the real estate owned by the domestic financial institution before the regional courts of the place where the assets are located, and the regional court has ordered the real estate to be frozen.

In the meantime, the legal person subject to the sanction has been authorised, under a discharge procedure authorised by the other Member State, to acquire a majority holding in the majority shareholder of the domestic financial institution established in that other Member State. The legal person on the sanctions list has sold its ownership interest to another legal person established in that Member State. As a result of the sale, the domestic financial institution ceased to have a

[28] 12-13 § of Act LII of 2017.

[29] 11. § of Act LII of 2017.

relationship with the sanctioned person and was, therefore, no longer indirectly subject to the sanction.

Based on the domestic financial institution's application, the national authority responsible for enforcing the sanctions found that the domestic financial institution could no longer be considered subject to the sanction as a result of the transfer of property following the discharge and, as a result, initiated an appeal before the courts to lift the blocking of the domestic financial institution's immovable property. The court found the application to be justified based on the business records of the domestic financial institution and its owners and lifted the freeze.

3. CIVIL LAW EFFECTS OF ECONOMIC SANCTIONS FOLLOWING THE JUDGMENT OF THE COURT OF JUSTICE OF THE EUROPEAN UNION IN CASE C-168/17[30]

The case law detailed below shows that economic sanctions can also apply to persons not subject to sanctions. It also illustrates how economic sanctions can influence the decision of a national court on a question of civil substantive law.

The case is based on applying the restrictive measures imposed by the EU in Regulation (EU) No 204/2011 in view of the situation in Libya, according to the UN Security Council Resolution. The sanctions prohibit the making available, directly or indirectly, of funds or economic resources of any kind whatsoever to or for the benefit of the natural or legal persons, entities or bodies listed in Annexes II and III to the Regulation and the making available of any claim in connection with the contracts or transactions concerned. The Regulation also provides an exception for payments due under contracts, agreements or obligations concluded before the date of designation. The definition of funds is defined in the Regulation by way of example, stating that funds are financial assets and economic benefits of every kind. It included, among other things, credit, right of set-off, guarantees, performance bonds and other financial commitments and letters of credit.

The legal relationship underlying the reference for a preliminary ruling was a settlement dispute between two Hungarian banks established in the EU. The dispute arose out of the provision of a counter-guarantee by a Libyan bank for a guarantee given to a Libyan customer in relation to the execution of a contract by a Hungarian company in Libya. During the legal relationship, the Libyan bank was subject to the above restrictions for a shorter period and the Libyan customer for a longer period, which resulted in a dispute over the EU banks' settlement obligations.

[30] Case C-168/17 *SH vs TG*, [2019], ECLI:EU:C:2019:36.

Before the national court, there was no doubt that as long as the Libyan customer was subject to sanctions, no counter-guarantee payment could be made in its favour. However, a preliminary ruling was required on whether the payment and enforcement of the various bank guarantee services and fees were subject to the prohibition and the temporal scope of the restrictive measures applicable to payments and settlement, which required an interpretation of EU law.

3.1. The Main Proceedings and the Legal Issues

According to the facts of the main proceedings, on 7 July 2009, HIB, a Libyan company, as the client, and UF, a Hungarian construction company, as the contractor, concluded a construction contract to construct several utility infrastructure improvements in Libya. The customer required Libyan bank guarantees in connection with the contract. The guarantees ensured that the contractor would perform against the advance payment received from the customer (advance payment guarantee) and that the works undertaken would be performed in accordance with the contract (performance guarantee).

Sahara Bank, a Libyan bank, provided the requested guarantees for the benefit of the Libyan contractor, but made this conditional on the existence of a counter-guarantee provided by a Hungarian bank.

The Hungarian contractor agreed with SH Hungarian Bank to provide the advance payment and performance counter-guarantee requested by the Libyan bank. SH provided the counter-guarantee through TG, also a Hungarian bank, by mandating TG to provide the counter-guarantee and standby letter of credit to the Libyan bank, and therefore, SH agreed to pay TG an advance commission of 1,30% per quarter and to reimburse the Libyan bank for its fees and costs, as well as its financing costs and any applicable default interest.

On 24 November 2009, TG issued to the Libyan bank a counter-guarantee for the repayment of the advance payment due on 30 August 2013 and, on 17 December 2014, an irrevocable standby letter of credit due on 30 June 2014. In respect of these, the Libyan bank issued the bank guarantees required by the Libyan customer in favour of the Hungarian contractor.

The Libyan companies involved in the relationship were added to the list of persons covered by the EU Regulation imposing restrictive measures because of the situation in Libya. The Libyan customer (HIB) was listed by name from 1 March 2011 to 29 January 2014, and indirectly, the Libyan bank (Sahara Bank) was listed temporarily from 22 March 2011 to 2 September 2011.

SH met its payment obligations to TG until March 2011. Between 2 September 2011 and 16 July 2013, the TG paid Sahara Bank the fees due under the counter-guarantee contract with it.

The two Hungarian banks agreed that SH, as the depositor, would deposit the unpaid guarantee fees but only pay them because the restrictive measures on HIB would be lifted until the expiry of these two counter-guarantees. It is stipulated that no request for payment of any advance repayment guarantee can be honoured as long as the HIB is subject to restrictive measures. The advance repayment counter-guarantee issued by SH expired on 14 September 2013, but the HIB has not been removed from the list in Annex III to Regulation 204/2011.

SH has applied to the court to substitute the defendant's statement of judgment for releasing the deposit under the deposit agreement. The defendant, TG, counter-claimed against SH for paying fees under a counter-guarantee agreement in various legal actions. The Court of First Instance upheld the action, upheld the counter-claim in part on contractual grounds and held that the guarantee fees due to TG in its own right did not fall within the scope of Regulation No 204/2011 since the case concerned the consideration for the services of TG, a Hungarian legal person. By contrast, the guarantee fees paid by TG to Sahara Bank indirectly served to discharge an obligation in favour of HIB, which is subject to Regulation 204/2011 and, therefore, falls within the scope of that Regulation and cannot be claimed from SH.

The Court of Appeal partially reversed the judgment of the Court of First Instance and dismissed the counterclaim in its entirety. It held that the parties had amended the provision in their guarantee agreement establishing the right to a premium and the due date, taking note of the situation created by the penalty. The payment was conditional on the removal of HIB from the blacklist by the date of expiry of the guarantees, which did not happen, and therefore, no fee was due to TG. It further pointed out that the sanction under the mandatory EU regulation made it impossible to enforce the claim in the civil law relationship, and therefore, TG could not provide the guarantee service and was not entitled to its remuneration.

TG applied for review to the Curia, which initiated a preliminary ruling procedure to interpret the contested EU law.

3.2. Decision of the Court of Justice of the European Union

In its judgment, the CJEU answered the questions referred for a preliminary ruling more precisely, grouping them differently from both the application and the Advocate General's Opinion. In the CJEU's view, the question referred by the referring court is whether Article 5(2) of Regulation No 204/2011, first, Article

12 of that Regulation, second, Article 9 of that Regulation and, fourth, Article 17(1) of Regulation No 2016/44, which replaced Article 12 of Regulation No 204/2011, apply to the dispute described.

In its answer to the rephrased first question on the applicability of Article 5(2) of Regulation 204/2011 to the dispute described, the CJEU went into detail on all three cases described in the question referred, namely the case of a bank guarantee provided by an EU bank to a Libyan bank subject to a restriction, the case of a bank guarantee provided by an EU bank to a Libyan bank not subject to a restriction but in favour of a restricted entity, and the case of payment of the fee for a counter-guarantee agreement between two EU banks.

In answering this question, ECJ has referred to its previous relevant case law to support a broad interpretation of the regulatory concepts applicable. According to that case, a prohibition on making funds or economic resources available to a person is to be interpreted broadly as covering all acts which, under the applicable national law, are necessary to exercise an effective and absolute right of disposal. The prohibition covers any disposal, whether or not it is an obligation arising out of the performance of a contract. Furthermore, the concept of funds and economic resources has a broad meaning, encompassing all assets, irrespective of the means of obtaining them.

In the first case, concerning the payment of a guarantee fee by an EU bank to a Libyan bank subject to the restrictions, the CJEU underlined that Sahara Bank was on the list on which the restrictions were based from 22 March to 2 September 2011. Because of this period, only Regulation 204/2011 was applicable. The CJEU interpreted the prohibition in Article 5(2) of Regulation 204/2011 to include the direct provision of funds to a bank listed in the list of persons subject to the prohibition, irrespective of the legal title. The scope of the prohibition is independent of the fact that the payment obligation is based on the performance of a contract concluded before the Regulation's entry into force, which establishes a balanced service and counter-service.

In the second case, the CJEU held that if the beneficiary of the premium under the counter-guarantee contract of the insured bank guarantee is not subject to the prohibition, such a payment does not constitute a direct provision of funds within the meaning of Article 5(2) of the Regulation. However, an indirect provision or use for his benefit may arise because of the beneficiary's identity, subject to the prohibition. The CJEU has interpreted the concepts of indirect disposition and use of funds for the benefit of a listed person in the specific case.

The CJEU referred to the third case, the award of fees for a counter-guarantee agreement between two EU banks, as explained in the previous two cases. These

fees cannot be considered direct provisions within the meaning of Article 5(2) of the Regulation, but indirect provision to or use for the benefit of a restricted person may also arise in these cases.

The CJEU gave a detailed answer to the second question, which was rephrased, as to whether Article 12 of Regulation 204/2011 applies to the dispute described, and if so, which version of the text covered all the eventualities. In its answer, it addressed all three cases referred to in the referral, namely the case of a bank guarantee provided by an EU bank to a Libyan bank subject to a restriction, a bank guarantee provided by an EU bank to a Libyan bank not subject to a restriction but in favour of a restricted entity, and finally the payment of a fee for a counter-guarantee agreement between two EU banks.

The CJEU has analysed Article 12 of the Regulation and its different wording due to legislative changes as a basis for answering this question. It pointed out that the scope of the provision covers contracts and transactions which are directly or indirectly subject, in whole or in part, to restrictive measures. The sanction contained in the provision, the prohibition of payment, is drafted by way of example and, therefore, covers all claims relating to the contracts and transactions concerned. Concerning the change of legislation, it pointed out that the original wording of Article 12 of Regulation 204/2011 referred to claims by the Libyan government and any person by or for the benefit of the Libyan government. The version under Regulation 45/2014, which entered into force on 22 January 2014, covered the persons listed in Annex II or III to Regulation 204/2011 and the claim of any person in Libya.

It found that both the counter-guarantor (Sahara Bank) and the guarantor (HIB) were subject to the restrictions and, on the other hand, the counter-guarantee fee payment claim, if it originated from a person specified in the provision, was subject to the restriction in the Regulation and therefore the applicability of Article 12 in the case at issue in the main proceedings was justified.

In the first and second cases, the CJEU pointed out, concerning the claim for payment of a guarantee fee by the Libyan bank, which was and was not subject to the restriction, that since the last payment was made under the original wording of Article 12, the scope of the restriction should be examined based on the original provision. He pointed out that whether the Libyan bank was subject to the restriction is relevant to the application of Article 12 and that it is for the national court to determine whether it was.

In the third case, the CJEU also examined the different versions of Article 12 concerning assessing the remuneration of the counter-guarantee agreement between two EU banks. The CJEU considered that, since the EU bank was paid the fee for the counter-

guarantee granted to the Libyan bank, the EU bank could not be deemed acting on the Libyan government's behalf. However, even an EU bank may be subject to the restriction under Article 12(c) of Regulation 45/2014 if it is a person on the list in Annex III to the Regulation, any Libyan person or the Libyan government.

The CJEU has also interpreted the contractual chain consisting of the bank guarantee and two counter-guarantees described in the leading case for the applicability of Article 12(c). According to this provision, the parties to a counter-guarantee contract are the principal (SH) and the counter-guarantor (TG). The remuneration for the counter-guarantee contract is the consideration for the service provided by issuing the counter-guarantee. The counter-guarantor is, therefore, not acting on behalf of the beneficiary (Sahara Bank).

The CJEU has given a clear answer to the third question, rephrased, as to whether Article 9 of the Regulation applies to the dispute described based on the facts provided. According to its interpretation, there is a material and a personal limit to the applicability of the exception rule in Article 9. The material limitation is that the payment is based on the consideration due under contracts, agreements or obligations concluded before the restriction. The personal limit is that the person entitled to receive the payment is listed in Annex II or III of the Regulation.

CJEU pointed out that in the leading case, there was no payment under the above conditions, as there was no payment at all to the listed HIB and no payment to Sahara Bank at the time of its listing. Therefore, the application of Article 9 cannot arise in the main case.

In response to the rephrased fourth question, the CJEU noted that Regulation 2016/44 entered into force on 20 January 2016 and that the provisions of Article 17(1) are essentially identical to the wording of Article 12(1) of Regulation 204/2011 under Regulation 45/2014. As regards the choice of the applicable Regulation, it attached importance to the date of the final settlement, according to which, since the fees paid by TG to Sahara Bank were paid before 20 January 2016, the previous Regulation applies. However, the final settlement has not yet occurred between the two EU banks, SH and TG, and therefore, the payment falling within the scope of Regulation 2016/14 is subject to this Regulation.

3.3. Ratio Decidendi

In the judgment, the CJEU clarified that the concept of funds under the Regulation is to be interpreted broadly, covering the type of guarantee undertaking not expressly mentioned in the illustrative list, the provision of counter-guarantees

and all fees and commissions incurred in connection with the provision of such guarantees, irrespective of their denomination.

The prohibition covers the direct or indirect provision of funds or economic resources to or for the benefit of a person subject to a restrictive measure. The judgment makes it clear that a direct payment to a person on the restricted list is prohibited. It is, however, for the national court to determine whether, where the recipient of the direct transfer is not subject to the prohibition, there is an indirect provision or provision for the benefit of the person subject to the prohibition. In this context, it is necessary to establish the legal and financial link between the prohibited person and the recipient of the funds. It is also required to verify whether the payment results in exercising a right by the prohibited person or, in the case of a claim, enforcing a guarantee.

For the non-execution clause, the provisions of the Regulation in force at the time of final settlement shall apply to the funds paid and to the amounts and claims not yet settled.

It is up to the national court to decide, on the basis of the rules of the relevant sanction regime and the facts of the case before it, whether the economic link which the legislator seeks to restrict exists.

4. THE IMPORTANCE OF THE ECONOMIC SANCTIONS IN CIVIL LAW CASES

The presented judgments draw attention to the need for national courts to remain vigilant in their proceedings to ensure that funds are not made available, directly or indirectly, by their nationals or by other persons present in their territory to persons subject to financial restrictions. This obligation is not limited to cases of direct provision, which can be easily verified based on up-to-date personal records, but requires a broader examination. For all claims involving funds or economic resources, it may be necessary to "vet" the identity and economic links of the eligible parties to identify the legal and financial link that may confer a right of disposal on the restricted persons. Furthermore, in the case of complex contractual chains, it is also necessary to examine to which person in the complex legal web the financial asset or economic resource which is the subject of the proceedings confers a right.

Enforcement of the Regulation is not limited to litigation in the courts but can also arise in non-litigation, whether in enforcement or non-litigation concerning the liquidation of assets. The Act LII of 2017 on the Enforcement of Financial and Property Restrictive Measures imposes an obligation on service providers and supervisory bodies subject to the Prevention and Suppression of Money Launder-

ing and Terrorist Financing Act. In addition, the courts and company courts are required to enforce the freezing of assets.

In light of the above, knowledge of the material scope and temporal scope of the asset freeze and economic restrictions is essential both in the substantive assessment of a dispute and in the decision on enforcement. This judgment has clarified for practitioners the applicable legal instruments and the analytical criteria necessary for their correct application, both in terms of the broad concept of funds and the assessment of payments and enforcement.

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