

## Commodity Finance Banks in Switzerland: Recommended Best Practices

Switzerland is the leading European center for commodity finance. Ten banks active in the field of Commodity Trade Finance (“CTF”) in Switzerland have worked to produce a summary of recommended best practices for their CTF activity. This initiative arose as a result of the significant losses experienced in a number of fraud or insolvency events that impacted the sector globally in the course of 2020, leading to a perceived need to strengthen and standardize market practice in the field of commodity finance. Good implementation of best practices by the relevant sectorial teams of each bank, and an on-going initiative to exchange views on these subjects of common interest are seen as useful tools to reduce the potential for future losses and deemed important to ensure the sustainability of CTF activities.

It is important to highlight that the adoption and implementation of such recommendations is voluntary, non-binding and remains at the full discretion of each bank, being subject to their respective internal processes and working guidelines. Each bank remains free to tailor the degree of adoption to the circumstances of its individual client relationships.

Recognizing differences in the modalities of trade and consequently specific finance practice between the various commodities, a general common practice was prepared and a summary of most of these recommended best practices can be found below.

**Below recommendations are for “Transactional and self-liquidating Financing”.**

Financing Stage	Summary of recommended Best Practices
Prefinancing	<ul style="list-style-type: none"> <li>- Prefinancing with payment directly to the producer or its trading arm and ideally confirmation of receipt of the funds by the supplier in such case.</li> <li>- Supplemental agreements/deeds of surety should be asked where possible, with repayment to named bank account in case of non-delivery.</li> <li>- No set-off or counterclaims clause shall be a standard.</li> </ul>
Refinancing	<ul style="list-style-type: none"> <li>- Reason for starting a transaction by refinancing to be clear.</li> <li>- Renunciation of Rights to be received if refinancing an original financing bank.</li> <li>- If refinancing from client’s (stated) self-financed position, Banks to:               <ul style="list-style-type: none"> <li>a) critically think about the plausibility given resources and financing model,</li> <li>b) receive evidence of payment made to original supplier and</li> <li>c) (other than Softs) notify the bank that made original payment, checking where justified whether they are financing the underlying.</li> </ul> </li> </ul>

<p>Inland Finance</p>	<ul style="list-style-type: none"> <li>- Pay direct to known supplier and monitor receipt at destination within expected time frame.</li> <li>- Banks to perform random checks on RWBs in case of receipt of dispatch list.</li> </ul>
<p>Voyage / BL Finance</p>	<ul style="list-style-type: none"> <li>- Banks shall perform random checks to confirm the genuine nature of Bills of Lading (IMB or similar).</li> <li>- BL should be to order of the financing bank, subject to market and transaction specificities.</li> <li>- Banks shall ensure an IT capability to track vessels and perform regular monitoring to ensure consistency with the expected voyage and timing.</li> </ul>
<p>Copy BL Finance</p>	<ul style="list-style-type: none"> <li>- Copies of BLs should ideally be issued to order of the bank (if voyage length allows delivery of originals for due endorsement) and even if not, financing against copies should generally be followed by receipt of the Original BLs at the bank.</li> <li>- If not followed by receipt of Original BLs at financing bank, a well-justified explanation must be provided beforehand to and accepted by the bank (e.g., short voyages).</li> <li>- Attention to be paid to BL date and no financing of copy BLs older than 10 days (30 days for crude cargo) from shipment date (“old” copy BLs being a red flag).</li> </ul>
<p>Inventory Finance</p>	<ul style="list-style-type: none"> <li>- Banks to have a procedure to approve warehouses.</li> <li>- Right for periodic third-party checks.</li> <li>- Banks to work to propose a standard form of questionnaire for warehouse / terminal Due Diligence.</li> <li>- Documents (WR, HC etc.) to be received directly from the warehouse with long run objective to verify genuineness of such documents via electronic platforms.</li> <li>- Periodic reconciliation with reconfirmation directly to/from warehouse.</li> <li>- In case of tenor extension at a minimum reconfirmation from warehouse and for longer tenors regular confirmations from third party inspectors.</li> <li>- Periodic sample checks by third parties, where justified.</li> <li>- Consider to alternate Inspection Companies or to mandate a one-off inspection from a different surveyor.</li> <li>- Where more than one bank is financing in the same storage location/ floating storage, consider arranging inspection of all financed material (same inspection company for all financing banks), detailing to each bank their specific quantity and referring also to the global result without necessarily revealing the detailed position of the other banks.</li> <li>- Consider arranging an Inter-creditor agreement where goods financed are comingled.</li> <li>- Consider (best practices) to take local pledges and legal opinions where inventory is sufficiently material and/or long- staying.</li> </ul>

Receivable Stage	<p>Bank should conduct adequate due diligence on open account counterparts.</p> <p>Financed contracts should be freely assignable; Banks should push for sales contracts to be assignable to financing banks without prior approval requirement from buyers.</p> <p>Sales contracts financed should be without set-off rights. Banks should identify and be fully aware when accepting financing against contracts with set-off rights.</p> <p>Client invoices should be required to be claused indicating that proceeds are assigned to the financing bank. Over a certain threshold, client to copy Bank in communication when submitting invoices directly to end buyers.</p> <p>Over a certain threshold (to be determined by each bank) banks should notify assignment directly to end buyers as an industry standard practice. In the energy sector such notification may be substituted by an acceptable Payment Undertaking communicated in advance.</p> <p>Banks to be systematically in copy of notice of assignment, Payment Undertaking and/or acknowledgement.</p> <p>Receivable only financing without full transactional financing to be subject to Refinancing criteria or be granted on very selective basis and after appropriate due diligence.</p> <p>Banks shall have the right to periodically confirm outstanding debtor balances with offtakers.</p> <p>Objective to ultimately verify genuineness of sales/invoices via electronic platforms, as alternatives to call back procedures or direct email from/to offtaker.</p> <p>Banks to abstain (and raise as a red flag) from financing circular transactions which aim at creating liquidity.</p> <p>Banks should regularly require and review debtor lists as part of the credit approval and review process.</p>
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### Borrowing Base (BB) Finance

Availability	Restricted to larger, more institutional clients, otherwise to be more transactional in nature of administration.
Independent checks	Annual third-party inspection of BB administration with sample testing commissioned by Security Agent.

## Instruments

Doc SBLCs	<ul style="list-style-type: none"> <li>- Banks should abstain to issue SBLCs in favour of unknown suppliers.</li> <li>- Banks to insist on a reference to underlying contracts in SBLC.</li> <li>- Banks to request systematically copy of shipping documents for payments in cancellation of SBLCs.</li> <li>- Wording of LOIs used for payments under SBLCs should stipulate that shipping documents are to be sent to client C/O (“care of”) the bank.</li> <li>- Should include a reduction clause.</li> </ul>
Non-Doc SBLCs	<p>As per Doc SBLCs plus:</p> <ul style="list-style-type: none"> <li>- Endeavor to limit usage to established suppliers.</li> <li>- Obtain a waiver from applicant or bank to send to the applicant a disclaimer (i.e indemnity to pay a seemingly on demand valid claim without further objection: wording at discretion of the bank) for SBLCs ruled under ISP 98.</li> </ul>
Letters of Indemnity	<ul style="list-style-type: none"> <li>- Banks to work to propose a LOI wording that would stipulate that shipping docs be sent to client C/O the bank (if supplier is not a major).</li> <li>- Non C/S LOI to be restricted only to Majors, Global Traders and NOCs.</li> <li>- In case a bank would be required by the charterer or carrier/ship owner to counter sign a discharge LOI, bank (at its full discretion) may agree to do it only if it is in a position to honor all terms notably as it comes to location and remittance of the B/L’s, otherwise the bank may decide to only accept discharge without taking further commitments.</li> </ul>

## Governance

Auditors and Accounts	<ul style="list-style-type: none"> <li>- Audit firm to be of sufficient size and reputation.</li> <li>- Consideration to rotate audit firm after 5 years. Or at least rotate audit partner when audit firm ranks among top 7.</li> <li>- Different auditor and/or closing dates within a group of companies owned by the same UBO is a potential red flag and to be critically assessed.</li> </ul>
Management	<ul style="list-style-type: none"> <li>- Attention should be paid to institutional checks and balances.</li> <li>- Banks should assess depth and independence of key management functions and non-executive directors.</li> <li>- Banks should consider as appropriate (in particular in cases of high growth in turnover or a material change in business model or ongoing important leverage between exposure at risk and financial recourse) to require operational audits / qualitative assessments by external consultants. Clients to potentially seek to optimize additional workload by requiring banks to combine into one audit.</li> </ul>
Location	<ul style="list-style-type: none"> <li>- Coherence between jurisdiction of client incorporation and substance of operation.</li> <li>- Preference for incorporation in jurisdictions with a sound and predictable legal system.</li> <li>- Encourage client to locate strategic center of decision and/or trade finance desk in Europe/Switzerland.</li> </ul>
Ongoing Learning & Training	<ul style="list-style-type: none"> <li>- Banks should conduct rigorous lessons learned exercises in case of loss and give periodic training to staff.</li> <li>- Staff (across the spectrum) should be trained to be sensitive to red flags and required to report red flag indicia or events.</li> </ul>

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