

May 19, 2020

## **U.S. Government Issues Updated Sanctions Compliance Guidance for the Maritime Industry**

On May 14, 2020, the U.S. Department of State, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC"), and the U.S. Coast Guard (collectively, the "Agencies") issued updated guidance entitled, "Guidance to Address Illicit Shipping and Sanctions Evasion Practices" (the "Advisory").<sup>1</sup> The Agencies state that "[i]t is critical that private sector entities appropriately assess their sanctions risk and, as necessary, implement compliance controls to address any identified gaps in their compliance programs,"<sup>2</sup> especially when operating in or near areas determined to be high risk.<sup>3</sup> Accordingly, the Advisory provides the maritime industry and energy and materials sectors with recommended compliance measures to counter current and emerging trends in illicit shipping and sanctions evasion, particularly with respect to Iran, North Korea, and Syria sanctions. Given OFAC's recent focus on pursuing enforcement actions involving violations caused by underlying compliance deficiencies, actors operating in these industries would be well advised to study the Advisory carefully to ensure that their compliance programs are consistent with the Agencies' expectations in order to mitigate their sanctions enforcement risk.

The intended audience for the Advisory includes U.S. and non-U.S. ship owners, managers, operators, brokers, ship chandlers, flag registries, port operators, shipping companies, freight forwarders, classification service providers, commodity traders, insurance companies, and financial institutions. In addition to highlighting general sanctions compliance best practices, the Advisory also suggests particularized compliance measures for each of these categories of actors. The Agencies also encourage companies and individuals involved in the supply chains of trade in the energy and metals sectors—including trade in crude oil, refined petroleum, petrochemicals, steel, iron, aluminum, copper, sand, and coal—to review the Advisory and enhance sanctions compliance programs as appropriate.

As with OFAC's May 2019 Framework for Compliance Commitments (the "2019 Framework"),<sup>4</sup> the Advisory reflects a new effort by the U.S. government to more clearly and comprehensively communicate its expectations about appropriate sanctions compliance practices. The Advisory acknowledges that compliance programs are inherently risk-based and will vary depending on a number of factors, but notes that each compliance program should be predicated on the five essential components highlighted in OFAC's 2019 Framework: (1) management commitment; (2) risk assessment; (3) internal controls; (4) testing and auditing; and (5) training.

U.S. and non-U.S. companies operating in the maritime and related industries should consider undertaking a critical risk-based assessment of their existing compliance policies against the standards expressed by the Advisory and, to the extent deficiencies are identified, implementing any necessary enhancements.

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### Identification of Deceptive Shipping Practices

As noted in the Advisory, approximately 90 percent of global trade involves maritime transportation, rendering the maritime industry an attractive and necessary target for illicit actions seeking to infiltrate and exploit global supply chains. The Advisory identifies the following seven tactics commonly utilized to evade sanctions:

1. **Disabling or Manipulating Vessel Automatic Identification Systems (“AIS”).** AIS is a mandated automatic tracking system that transmits vessel identification and navigational positional data via high frequency radio waves. The practice of manipulating AIS data, referred to as “spoofing,” allows ships to broadcast inaccurate identifying information, such as vessel name, International Maritime Organization (IMO) number, or Maritime Mobile Service Identity.
2. **Physically Altering Vessel Identification.** Illicit actors have often painted over vessel names or IMO numbers to obscure their identities or impersonate other vessels.
3. **Falsifying Cargo and Vessel Documents.** Authorities have found that sanctions evaders have falsified shipping documentation, particularly with respect to petrochemicals, petroleum, petroleum products, metals (steel, iron), or sand in order to disguise their origin. Falsification of records is illegal in most countries and irregularities may provide a basis to hold a shipment until contents are validated. The Agencies encourage due diligence on documents that suggest cargo is from a high-risk geography.
4. **Ship-to-Ship Transfers.** Especially when undertaken in areas determined to be high-risk for illicit activity or at night, ship-to-ship transfers are frequently used as a mechanism to conceal the origin or destination of cargo, particularly with respect to petroleum, coal, and related materials.
5. **Voyage Irregularities.** Illicit actors may attempt to disguise the ultimate destination or origin of cargo or recipients by using indirect routing, unscheduled detours, or transit or transshipment of cargo through third countries. The Agencies encourage private sector actors to scrutinize voyages that deviate from normal practice.
6. **False Flags and Flag Hopping.** Illicit actors may falsify vessel flags or repeatedly register with new flag states to avoid detection. The Agencies recommend that the private sector report such behavior to the relevant authorities.
7. **Complex Ownership or Management.** Illicit actors may utilize complex business structures and shell companies to disguise beneficial ownership of cargo or commodities; the private sector should be mindful of a pattern of changes in ownership or management companies. If private sector

entities are unable to reasonably identify the real parties in interest in a transaction, they may wish to consider performing additional due diligence.

The Agencies advise that companies operating in the maritime sector should be vigilant against these tactics to limit the risk of involvement in illicit or sanctionable activity, and that heightened due diligence be exercised with respect to shipments transiting areas deemed to present high risk.

### **General Practices for Effective Identification of Sanctions Evasion**

The Agencies recommend private sector actors consider adopting the following seven general business practices in order to more effectively identify potential sanctions evasion.

1. **Institutionalize Sanctions Compliance Programs.** As appropriate, assess sanctions risk, implement sanctions compliance and due diligence programs, and provide training and resources to personnel in order to best execute those programs. Companies continue to be encouraged to develop, implement, and adhere to written standardized operational compliance policies, procedures, standards of conduct, and safeguards. The Advisory suggests establishing that engaging in sanctionable conduct is cause for termination, and highlights as a best practice that employees raising compliance concerns be shielded from retaliation and that a confidential reporting mechanism exist. Companies may wish to have their sanctions programs audited by qualified third parties as a means of continuous improvement. Finally, sanctions compliance practices may include communicating to counterparties an expectation that such counterparties also have adequate and appropriate compliance policies, including controls that comport with the Advisory.
2. **Establish AIS Best Practices and Contractual Requirements.** Entities in the maritime industry may wish to consider researching a ship's history to identify previous AIS manipulation and monitoring AIS manipulation and disablement when cargo is in transit, as well as promoting continuous broadcasting of AIS throughout the life of a transaction, especially in those areas determined to pose a high risk for sanctions evasion. Financial institutions may also—as appropriate—implement relevant controls for their maritime industry clients, particularly those that own, operate, and/or provide services to ships operating in areas determined to pose a high risk for sanctions evasion. Service providers may wish to consider amending contracts to make disabling or manipulating AIS for illegitimate reasons grounds for termination of contracts. Finally, parties could consider incorporating contractual language that prohibits transfers of cargo to client vessels that are not properly broadcasting AIS or that have a suspect AIS history.
3. **Monitor Ships Throughout the Entire Transaction Lifecycle.** Ship owners, managers, and charter companies are encouraged to continuously monitor vessels, including those leased to third parties. This could include supplementing AIS with Long Range Identification and Tracking and

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raising awareness of common deceptive practices among vessel operators that conduct ship-to-ship transfers in areas determined to be high-risk. Industry actors may also consider looking for situations where ownership of a vessel is transferred between companies controlled by the same beneficial owner without a discernable legitimate purpose. As we described in a previous memorandum, monitoring leased assets over the lifecycle of the transaction is a theme that OFAC recently highlighted in its settlement with Apollo Aviation.<sup>5</sup>

4. **Know Your Customer/Counterparty.** Flag registry administrations, insurers, financial institutions, managers, and charterers should continue to conduct risk-based due diligence as appropriate. This due diligence might include maintaining the names, passport ID numbers, address(es), phone number(s), email address(es), and copies of photo identification of each customer's beneficial owner(s).
5. **Exercise Supply Chain Due Diligence.** Companies across the maritime supply chain are encouraged to conduct appropriate due diligence as relevant to ensure that recipients and counterparties to a transaction are not sending or receiving commodities that may trigger sanctions. This may include verification of origin and recipient checks for ships that conduct ship-to-ship transfers, requesting copies of applicable export licenses, and complete shipping documentation. Companies are also encouraged to review the details of an underlying voyage, including the vessel, cargo, origin, destination, and parties to the transaction, and, consistent with their internal risk assessment, to review the relevant documents to ensure that the underlying goods were delivered to the port listed in the documentation and not diverted in an illicit or sanctions-evading scheme.
6. **Contractual Language.** Companies are encouraged to incorporate these compliance best practices in their contract documents.
7. **Industry Information Sharing.** The Agencies recommend that maritime industry groups encourage members to provide relevant information and share it broadly with partners, other members, and colleagues consistent with applicable laws and regulations. For example, if an insurance company becomes aware of new tactics in sanctions evasion, it may consider notifying similarly situated insurers to the extent permissible under applicable law. Likewise, vessel owners and clubs are encouraged to share information with the financial industry, working through competent authorities where required, and flag administrations should routinely pass information to the IMO and parties to the Registry Information Sharing Compact.

Companies would be well served to consider how these practices might be leveraged to enhance their risk-based due diligence and compliance programs.

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### Organization Type Specific Guidance

In addition to the general compliance recommendations described above, the Advisory contains an annex with tailored guidance for nine types of organizations operating in the maritime industry: (1) maritime insurance companies (pp. 9-10); flag registry managers (pp. 11-12); port state control authorities (p. 13); shipping industry associations (p. 14); regional and global commodity trading, supplier, and brokering companies (pp. 15-16); financial institutions (p. 17); ship owners, operators, and charterers (p. 18); classification societies (p. 20); vessel captains (p. 22); and crewing companies (p. 23).

For example, the Advisory states that financial institutions should rely on their internal customer risk assessments to employ appropriate risk mitigation measures consistent with applicable money laundering and counter-terrorism laws and regulations, including, where applicable, FinCEN's customer due diligence and beneficial ownership requirements.<sup>6</sup> The Agencies suggest that such assessments include, in part, consideration of the following risk factors:

- Identifying commodities and trade corridors susceptible to transshipment and ship-to-ship transfers and the extent of their use by a customer;
- Assessment of the nature of a client's business, including the type of services offered and geographical presence;
- Activity inconsistent with clients' typical business practices (including when clients acquire new vessels); and
- Client acquisition or sale of vessels to determine that the client's assets do not include blocked property.

Financial institutions and other companies operating in the maritime or related industries would be well served to carefully review the specific guidance areas applicable to their operations and incorporate the Agencies' recommendations into their compliance programs, as appropriate, based on their own sanctions risk assessments.

We will continue to monitor sanctions developments and look forward to providing you with further updates.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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<sup>1</sup> U.S. Dep't of the Treasury, Office of Foreign Assets Control, U.S. Department of State, and U.S. Coast Guard, Guidance to Address Illicit Shipping and Sanctions Evasion Practices (May 14, 2020), available [here](#).

<sup>2</sup> *Id.* at 1.

<sup>3</sup> The Advisory also updates and expands prior country-specific shipping advisories issued by OFAC pertaining to Iran, North Korea and Syria, and includes as an Annex information about the sanctions programs targeting these regimes, including the bases for designation by the U.S. government. *See* Advisory Annex B.

<sup>4</sup> U.S. Dep't of the Treasury, Office of Foreign Assets Control, A Framework for OFAC Compliance Commitments, (May 2, 2019), available [here](#); *see* Paul, Weiss, OFAC Issues Guidance on Sanctions Compliance Programs and Flags "Root Causes" Underlying Prior Enforcement Actions (May 14, 2019), available [here](#).

<sup>5</sup> Paul, Weiss, OFAC Enforcement Action against U.S. Aviation Company Shows the Importance of Ongoing Monitoring over the Course of a Contractual Relationship (Dec. 9, 2019), available [here](#).

<sup>6</sup> Advisory at 17.