# 5 Ways Maritime Cos. Can Enhance Sanctions Compliance

By **Jeffrey Orenstein and Catherine Johnson** (October 23, 2023)

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Recent reports show that illicit and deceptive shipping practices, designed to evade economic sanctions, are at an all-time high.

On Oct. 12, for example, addressing widespread evasion of the Russian oil price cap, the U.S. Department of the Treasury's Office of Foreign Assets Control published an advisory and sanctioned certain vessels.[1]

It is imperative, therefore, that all companies engaged in maritime shipping — particularly vessel owners and operators, charterers, commodity traders, brokers, and insurers — address the considerable risks they face under U.S., EU, and U.K. economic sanctions.

The magnitude of these risks is reflected in the fact that more than 750 vessels and 800 companies engaged in maritime shipping are currently on the Specially Designated Nationals and Blocked Persons List, administered by OFAC. Civil and criminal penalties are also on the rise, with one case of EU violations resulting in fines exceeding $50 million.

While most companies conduct some sanctions screening, simple searches of the sanctions lists are not nearly enough to address the risks of dealing — directly or indirectly — with restricted parties, countries and cargos.

Failure to conduct sufficient due diligence can lead not only to high monetary penalties, but also to crippling blocking sanctions, costly litigation, contractual damages, vessel arrests, government seizures, suspended operations and even criminal prosecution.

This article discusses the top five factors to consider when conducting due diligence for sanctions purposes. It also provides real-world examples of both the legal and commercial consequences companies have suffered when sanctions compliance efforts fell short.

**1. Applicability of Sanctions**

Every transaction in international trade has the potential to implicate one or more sanctions regimes. It is essential, therefore, to understand each regime's jurisdictional reach, its restrictions and how it applies them to specific transactions and parties.

Example: A Cypriot commodity trader bought a cargo in U.S. dollars and chartered a vessel insured by an English protection and indemnity insurance club. In this case, the parties involved had compliance obligations and risks under EU, U.K., and U.S. sanctions.

Example: OFAC designated several European-owned vessels and owners on the SDN list after they carried Venezuelan crude to Asia. Some owners had failed to understand that such voyages could trigger U.S. blocking sanctions — even when there were no U.S. persons, U.S. dollar payments or other U.S. nexus involved.

**2. Restricted and High Risk Parties**

The first step to sanctions screening is to confirm no parties involved in a transaction are on restricted party lists. However, that is only a first step.

Under U.S. sanctions, an entity will be blocked not only if it is named on the SDN list, but also if it is owned 50% or more by parties on the SDN list. Similarly, under EU and U.K. sanctions, restrictions may apply if an entity is owned or controlled by a sanctioned party.

It is necessary, therefore, to screen each party involved, and the parties who own and control each party. Due diligence should also include consideration of whether a party is a likely sanctions target due to its past sanctionable business dealings.

Example: OFAC imposed a substantial monetary penalty on a company for making three shipments of goods to a Russian entity that was not named on any restricted party lists, but was nevertheless blocked because it was owned 51% by a Russian company on the SDN list.

Example: A tanker was unable to discharge and remained at sea for over six months after OFAC designated the cargo owner on the SDN list mid-voyage. Although the cargo owner was not sanctioned when the vessel was chartered, the cargo owner's involvement in Iran's petrochemical trade made it a likely sanctions target.

Due to these sanctions, the vessel was burdened with a blocked cargo it could not discharge. The vessel owner incurred substantial costs from lost hire, multiple vessel arrests by parties claiming the cargo, a charterparty dispute, and accumulated legal fees.

**3. Sanctioned Countries and Front Companies**

Even if the parties to a shipment are not designated on any restricted party lists, or owned or controlled by restricted parties, sanctions may nevertheless apply if a party is organized, located or owned by parties in a sanctioned country.

U.S. sanctions, for example, prohibit most commercial dealings involving — directly or indirectly — Cuba, Iran, North Korea, Syria and certain regions of Ukraine. Broad U.S. sanctions also apply to Russia and Venezuela.

To avoid such country-based restrictions, owners should confirm each party's national affiliations, as well as that of their beneficial owners, and be alert to intermediaries and front companies in nonsanctioned countries that operate on behalf of parties in sanctioned countries.

Recently formed companies with minimal public presence warrant further diligence to understand their true ownership, affiliations and operations.

Example: U.S. authorities are currently investigating both U.S. and non-U.S. companies for shipments of goods to recently formed EU companies that act as fronts for the Iranian and Russian governments in their efforts to obtain western goods for their military programs.

Example: Danish authorities criminally convicted a Danish company, its parent and its CEO, imposing millions of dollars in fines, for selling jet fuel to companies that transferred the fuel to Syria in violation of EU sanctions. The prosecutor made clear that "even negligence can lead to a conviction, and the defendants should have analyzed what was going on much more thoroughly."

Example: A company paid over $1.5 million to settle its liability for selling and shipping goods to an Indian buyer who resold the goods to Iran. Although the buyer was not Iranian and was not a restricted party, its principal business was the distribution of goods in Iran. Accordingly, OFAC found that the seller either knew or should have known the goods were destined for Iran.

**4. Cargo Diligence**

A cargo's country of origin and past ownership can present sanctions risks for those buying, selling or transporting the cargo. The true origin of commodities from Iran, North Korea, Russia and Venezuela is routinely disguised using false certificates, transshipments, blending operations, front companies, intermediaries and deceptive shipping practices.

Regulators have imposed heavy fines and sanctions on companies that fail to conduct risk-based due diligence on the origin of cargo when they should have known a cargo's origin. With regard to the Russian oil price cap, cargo diligence may require consideration of both a cargo's origin and its pricing.

Example: U.S. authorities seized a cargo of crude oil loaded by a European-operated vessel in a ship-to-ship transfer near Singapore upon discovering that the crude was Iranian origin. The charterer had disguised the origin of the oil using falsified documents, STS operations and automatic identification system manipulation.

Although the parties were not U.S. persons, the charterer used the U.S. financial system to facilitate the shipment, thus violating U.S. sanctions. The vessel operator was criminally prosecuted and required to transport the seized cargo from Singapore to the U.S. at its own expense.

Example: OFAC designated a non-U.S. ship broker and its CEO on the SDN list after they fixed a vessel to carry to China petroleum products that were Iranian origin.

In court proceedings, the ship broker stated they do "not inquire about the cargo country of origin" and "often lack visibility" into the details of the contracts underlying the deals they broker. Nevertheless, U.S. authorities found that they either knew or should have known that they were facilitating the transportation of Iranian-origin cargo.

Example: A European vessel owner narrowly avoided the seizure of its vessel by the U.S. government when U.S. authorities alerted the owner to satellite imagery proving the oil the vessel was about to load in Basra, Iraq was actually Iranian-origin. Although charterers had provided documentation certifying the oil as Iraqi-origin, proper due diligence would have raised red flags indicating the cargo might be Iranian.

**5. Vessel Diligence**

Due diligence is just as important with regard to vessels as it is for parties. Screening should include a search of sanction lists for both the name and the International Maritime Organization, or IMO, number of the vessel.

It is also important to review the vessel's historical movements, and to look out for deceptive practices designed to disguise a vessel's identity, ownership or past positions.

In addition to renaming vessels, these deceptive practices include:

- Flag falsification;
- Repeated registration with new flag states — known as flag hopping;
- New ownership structures;
- Alteration of vessel identification — e.g., painting over vessel names and IMO numbers; and
- Modification of a vessel's appearance — e.g., repainting and covering vessel features with tarpaulin.

Example: Turkish port authorities prohibited a vessel from discharging its cargo because it was discovered that the vessel was blocked under U.S. sanctions.

Prior to the vessel's charter, the vessel became blocked when OFAC designated its then-owner on the SDN list. The sanctioned owner subsequently sold the vessel to a nonsanctioned owner who renamed it.

Unfortunately for the charterer, the vessel remained blocked because the sale of a vessel does not unblock it. Rather, vessels remain blocked until OFAC grants a petition to unblock them.

Example: Spanish authorities barred a Singapore-flagged tanker from unloading its cargo because it was being used to evade EU restrictions on Russian-flagged vessels.

The vessel had loaded the cargo via STS transfer with a Vietnamese tanker, which received the cargo via STS transfer with a formerly Russian-flagged tanker. The Russian vessel had been sold and reflagged in Cameroon to evade EU sanctions.

Ultimately, the Singapore vessel spent two months at sea trying to unload its cargo, and Spanish authorities later detained the Vietnamese tanker and imposed a $130,000 fine.

Example: OFAC imposed civil penalties on a company for providing fuel inspection services to five blocked vessels. The names of the vessels had been changed, but the IMO numbers remained the same, making it easy for the fuel inspector to screen the vessels on the SDN list.

**Conclusion**

The real-world examples described above highlight the need for enhanced due diligence by all companies involved in maritime shipping. Merely searching for parties on sanctions lists is not sufficient to limit the serious legal and commercial risks posed by economic sanctions in the shipping sector.

Accordingly, the best practice is to develop and implement due diligence procedures that account for the types of sanctions issues raised by a company's specific operations, and assess each shipment, using tools that help evaluate the risks and sanctions status of all parties, countries, cargos and vessels.

It is equally important to adopt sanctions provisions for charterparties, purchase agreements and other contracts to manage sanctions risks and assign liability.

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[1] https://ofac.treasury.gov/media/932201/download?inline.