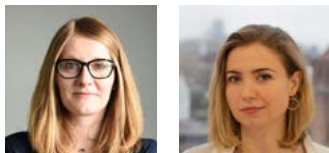




Maritime sanctions: Tips for due diligence



The world of due diligence in the maritime space has increasingly become the front line in tackling sanctions evasion. OFAC and OFSI advisories in 2020 made it clear that financial institutions are required to complete appropriate due diligence in the maritime space. **Paulina Izewicz** and **Cristina Rotaru** offer some top tips for financial institutions on how to recognise potential sanctions evasion.

Until fairly recently, international shipping has largely escaped scrutiny of sanctions enforcement. This began changing in recent years, and the focus appears poised to grow even further. The pre-JCPOA Iran sanctions regime, for instance, contained a maritime component, but it was not until the expansion of the North Korea sanctions regime starting in 2016 that maritime sanctions have really begun to take hold. This has been accompanied by increased attention from regulators. Since 2018, the US government has published six maritime advisories, the last of which received the most attention – the so-called Global Maritime Advisory issued in May 2020. This was followed by the publication, in December of the same year, of Maritime Guidance, by the UK's Office of Financial Sanctions Implementation ('OFSI').

Both the US and UK advisories make clear that the interplay between the maritime element of sanctions and global trade – an estimated 80% of which travels by sea – requires action

by all involved, at all stages of the transaction. From the FIs involved in the financing of vessels and cargo, to insurers and re-insurers, to companies using vessels to transport their goods, shipowners, charterers, and those providing maritime services such as classification, certification, bunkering, and so on. The recently updated proliferation finance guidance from the Financial Action Task Force ('FATF') also focuses on maritime trade, signaling increased attention to the problem and making it clear that a key way to identify and prevent proliferation finance is for all involved in trade to pay attention to maritime sanctions and shipping practices.

For FIs, it has always been best practice to understand the travel routes of imports and exports in order to manage and mitigate potential sanctions risk. The new compliance standards set by the advisories, however, make this more explicit and much more detailed, as well as setting out new due diligence requirements. The 2020 US Global Maritime Advisory, for example, in a section aimed

specifically at FIs, recommends identifying commodities and trade corridors susceptible to sanctions evasion activities (e.g., transshipment, ship-to-ship transfers), and how a FI's customers use them. This, of course, is only one element of the extensive due diligence required. To truly protect themselves against the risks involved in maritime sanctions, FIs need to understand how these measures apply to them, how sanctions evaders try to circumvent them, and how to conduct the sort of due diligence capable of catching it.

As the attention to maritime trade grows, sanctions evasion measures grow more and more sophisticated. Caught between these two trends, FIs face unprecedented risk, often with little experience and guidance on how to mitigate it. While using specialist companies and AI software solutions offer one, but by no means the only, potential solution, good understanding of sanctions evasion techniques can go a long way toward mitigating risk. Some of the answers can be found when examining case studies of sanctions evasion



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and enforcement action against vessels and those involved in the financing or servicing of these vessels and their cargos.

One recent enforcement case, involving unprecedented civil asset forfeiture against a North Korean vessel, the *Wise*

Honest, offers a clue-rich case study to draw out some practical tips for maritime due diligence.

In 2016-2018, Songi Trading Company, a company controlled by the North Korean regime, used the vessel *Wise Honest* to deliver UN-sanctioned North Korean coal to foreign buyers.¹ In March 2018, the ship set off on what was to be its final voyage: from the North Korean port of Nampo to Indonesia, a destination that one set of falsified cargo documents claimed was the origin of the coal onboard. Before it could transfer its illicit cargo to another vessel, however, the *Wise Honest* was detained by Indonesian authorities and subsequently handed over to the United States. Because some payments related to the ship's operations passed through

the US financial system, the US government was able to assert jurisdiction and take ownership of the vessel through civil asset forfeiture. The *Wise Honest* was then sold off for scrap, with funds used to provide compensation for the families of the victims of the North Korean regime, including the family of Otto Warmbier.²

Shell companies

The registered owner of the *Wise Honest* was Korea Songi Shipping Company, an affiliate of Korea Songi General Trading Corporation.³ While the North Korea connection was obvious because the ship sailed under the North Korean flag, and should have been sufficient to prevent anyone from doing business with it, the use of Korea Songi Shipping Company as the nominal vessel owner also obscured its real control – by

the Office of Foreign Assets Control ('OFAC')-sanctioned Korea Songi General Trading Corporation.

Tip: Information that appears incomplete, inconsistent, or contradictory may suggest illicit activity, and offers useful hints that can be pursued further. According to the forfeiture complaint, hints of the connection between the companies could have been discerned from a few sources. For example, some of the communication sent by the Korea Songi Shipping Company representative actually came on the letterhead of Korea Songi General Trading Corporation. The two companies also share the same address in Pyongyang, North Korea.

Tip: The company's name can also offer a valuable piece of information. North Korean

companies, including those registered abroad, often follow a particular naming convention: the word 'Korea', a Romanised Korean word (e.g., 'Songi'), and a variation of 'Shipping Company', 'Trading Corporation', 'General Trading', etc.

Front companies

A company called Hong Kong Nova International Trade Company was named in the contract as the seller of cargo onboard the *Wise Honest*.⁴ During the investigation by the UN Panel of Experts ('PoE') on North Korea, the body in charge of monitoring the implementation of the UN sanctions regime, the company claimed to have no knowledge of the deal. Wittingly or unwittingly, it acted as a front for illicit North Korean business.

Tip: Conduct know your customer ('KYC') checks on all parties to a transaction, and be on alert for any inconsistencies. In this case, had the cargo's buyer conducted due diligence on Nova International, it may have questioned why a company whose normal business was trade in cigarette manufacturing equipment was selling it coal. In addition to establishing the company's normal line of business, also verify its online presence (e.g., does it have a website, social media profiles? Are those in line with the transaction in question? Are there any inconsistencies about the online presence that make it look not quite 'right?'), its contact and address information (e.g., is the information complete? If not, does the company provide it upon request? Is the address shared with any other entity? Is the address where you would expect it to be when checking it via Google Street View? Is the timestamp in email communication consistent with where the company purports to be?), and banking information where available (e.g., does the company have an account with the sanctioned FI? Is

Due Diligence Resources

- IMO GISIS: www.gisis.imo.org
- Equasis: www.equasis.org
- List of UN-designated vessels (North Korea; separate from the persons/entities list): <https://www.un.org/securitycouncil/sanctions/1718/materials/1718-Designated-Vessels-List>
- Reports by the UN Panel of Experts on North Korea: https://www.un.org/securitycouncil/sanctions/1718/panel_experts/reports
- UN Implementation Reports (North Korea): <https://www.un.org/securitycouncil/sanctions/1718/implementation-reports> (see: Togo, Panama)
- Tanzania/Zanzibar circular listing vessels deregistered for links to North Korea: <https://www.zma.go.tz/Notices/Circular%20No.%20FSI%2001.2017.pdf>
- US government advisories (some include various 'grey' vessel lists):
 - February 2018: https://home.treasury.gov/system/files/126/dprk_vessel_advisory_02232018.pdf (North Korea)
 - November 2018: https://home.treasury.gov/system/files/126/syria_shipping_advisory_11202018.pdf (Syria)
 - March 2019: https://home.treasury.gov/system/files/126/syria_shipping_advisory_03252019.pdf (Syria)
 - March 2019: https://home.treasury.gov/system/files/126/dprk_vessel_advisory_03212019.pdf (North Korea)
 - September 2019: https://home.treasury.gov/system/files/126/iran_advisory_09032019.pdf (Iran)
 - May 2020: https://home.treasury.gov/system/files/126/05142020_global_advisory_v1.pdf (Iran, North Korea, Syria)
- UK OFSI Maritime Guidance: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/948299/OFSI_Guidance_-_Maritime_.pdf

Structured Google searches:

- "[full/partial company name]" AND "North Korea" / "Iran" / etc.
- "[address/email/telephone number]" AND "North Korea" / "Iran" / etc.
- "[vessel current and past name/IMO number]" "North Korea" / "Iran" / etc.

the FI located in a 'risky' jurisdiction? Does it match where the company is purportedly located?)

Tip: The reports published twice annually by the North Korea PoE are a great source of information. Many other UN sanctions regimes are supported by panels or groups of experts that also provide reports regarding their specific regimes. While some of their investigations may not result in a sanctions designation at the UN level, often for political reasons, the high evidentiary standard of these reports makes the information provided in them highly valuable for due diligence.

Foreign facilitators

Sanctions evaders are also known to utilise foreign facilitators, to further obscure ties to sanctioned entities or jurisdictions. In this case, the transaction was brokered by an Indonesian individual, brought into the scheme by the president of the OFAC-

designated North Korean bank, Jinmyong Joint Bank, to whom he was introduced by diplomats at the North Korean embassy in Jakarta.⁵ The broker used a Hong Kong-based company to charter the receiving vessel for the ship-to-ship transfer, the *Ken Orchid*.

Tip: While checks on the Indonesian broker may not have revealed links to North Korea, details of the transaction for which he planned to use the chartered vessel would have done so. *Wise Honest* was a North-Korea-flagged vessel, which means that any ship-to-ship transfers with it were prohibited by UN sanctions. If the details of the transaction are not provided or appear incomplete or suspicious in any way, requests for information ('RFIs') or a clarification may be necessary.

Tip: North Korean diplomats are known to be involved in illicit activities on behalf of the regime. They can register companies, open bank accounts, or

facilitate transactions. In one memorable case, concerning a shipment of tank components and other conventional arms to the Republic of Congo, the counsellor at the North Korean embassy in Brazzaville was even named as the addressee on the bill of lading.⁶ When presented with names common in specific regions that may be subject to sanctions, enhanced due diligence is essential.

Flag hopping, fraudulent flag use, unknown flag

The *Wise Honest* was seized with two sets of registration documents onboard – one from North Korea and one from Sierra Leone, where it was registered until 2016; it also at one point claimed registration with Tanzania,⁷ which had deregistered it in 2016 for links to North Korea.⁸ Following this period of changing flags, apparently unable to find registration elsewhere, the ship then took on the North Korean flag.

Tip: Verify information transmitted via Automatic Identification System ('AIS') with official International Maritime Organisation ('IMO') records, and vice versa; these are available in the official IMO database, the Global Integrated Shipping Information System ('GISIS'), or through the European Union-run Equasis, which among others ingests IMO data. The IMO has introduced a new flag marker for instances of fraudulent flag use (e.g., 'Micronesia FALSE'). As of this writing, the following registries have fallen victim to fraudulent flagging practices: Belize, Bolivia, Democratic Republic of Congo, Equatorial Guinea, Fiji, Kiribati, Maldives, Micronesia, Mongolia, Nauru, Palau, Sao Tome and Principe, Sierra Leone, Tanzania, Timor Leste, and Zambia.

Tip: Efforts in recent years have led to many North Korea-linked vessels being deregistered by open registries. Some of them have published lists of such deregistered ships or included

them in their implementation reports submitted to the UN Security Council (e.g., Tanzania, Togo, Panama – see box, 'Due Diligence Resources'). There may also be media reports about such instances. Some of those ships have taken the North Korean flag; others sail without any flag whatsoever – a red flag in its own right.

Ship-to-ship transfers

While ship-to-ship transfers may be conducted for legitimate reasons (e.g., wanting to avoid port fees, or the vessel being too big for a particular terminal), they have also become a sanctions evasion mainstay which serves to obscure the origin or destination of cargo. That cargo is most often petroleum products, but other restricted commodities, such as coal and sand, have also been transferred in this fashion.

Tip: Depending on the sanctions regime they are intended to bypass, ship-to-ship transfers often happen in a particular set of locations. For sanctions targeting North Korea, these transfers typically happen in the Yellow Sea, Sea of Japan, East China Sea, and the Gulf of Tonkin – for the exact spots, see the map included in OFAC's March 2019 maritime advisory (see box, 'Due Diligence Resources'). For sanctions concerning Iran and Venezuela be on alert for activities taking place off the UAE port of Fujairah, various locations off the African coast, Malaysia, Indonesia, and the Caribbean.

Tip: Monitoring vessel activity in these location can be helpful, particularly in combination with certain activity markers. For instance, AIS may be disabled for a few days in a known ship-to-ship transfer zone. Or a vessel repeatedly leaves and returns to the same port within a short period of time, or appears to be shuttling between a port and a known ship-to-ship transfer zone. This may be accompanied by draft changes, particularly at

Links and notes

- ¹ *United States of America v The Wise Honest*, Case 1:19-cv-04210-PKC, 21 October 2019, <https://www.justice.gov/opa/press-release/file/1211941/download>.
- ² Sam LaGrone, 'North Korean Cargo Ship Sold to Compensate Families of Regime's Victims,' USNI News, 9 October 2019, <https://news.usni.org/2019/10/09/north-korean-cargo-ship-sold-to-compensate-families-of-regimes-victims>.
- ³ *United States of America v The Wise Honest*.
- ⁴ UN Panel of Experts Report S/2019/171, <https://undocs.org/S/2019/171>.
- ⁵ *Ibid.*
- ⁶ UN Panel of Experts Report S/2015/131.
- ⁷ *Ibid.*
- ⁸ Circular No. 01/2017, Zanzibar Maritime Authority, 19 January 2017, [https://www.zma.go.tz/Notices/Circular No. FSI 01.2017.pdf](https://www.zma.go.tz/Notices/Circular%20No.%20FSI%2001.2017.pdf).
- ⁹ UN Panel of Experts Report S/2019/691, <https://undocs.org/S/2019/691>.
- ¹⁰ UN Panel of Experts Report S/2018/171, <https://undocs.org/S/2018/171>.
- ¹¹ United States Department of Justice, 'US Government Seizes Oil Tanker Used to Violate US and U.N. Sanctions Against North Korea,' 23 April 2021, <https://www.justice.gov/usao-sdny/pr/us-government-seizes-oil-tanker-used-violate-us-and-un-sanctions-against-north-korea>.
- ¹² Mikhail Voytenko, 'Chinese tanker seized by Cambodia, suspect in DPRK sanctions violation,' FleetMon, 2 March 2020, <https://www.fleetmon.com/maritime-news/2020/28981/chinese-tanker-seized-cambodia-suspect-dprk-sancti/>.
- ¹³ UN Panel of Experts Report S/2019/171, <https://undocs.org/S/2019/171>.

sea, indicating that cargo has been taken on or discharged through a ship-to-ship transfer.

AIS gaps and manipulation

The AIS onboard the *Wise Honest* had been off since August 2017, hiding its illicit activities. Had the Indonesian authorities not detained the *Wise Honest*, its ship-to-ship transfer with the *Ken Orchid* almost certainly would have happened in an AIS blackout as well.

Tip: While AIS gaps can happen for legitimate reasons (e.g., signal interruptions due to particularly dense traffic, fears of piracy), repeated, prolonged, and unexplained gaps in particularly sensitive locations, as well as unusual transmissions should be cause for further investigation. Gaps in AIS transmissions can be verified through LRIT or Inmarsat data, as appropriate, but usually will need to be judged on a case-by-case basis, taking into account vessel type, its area of operations, its cargo, and any other red flags the vessel itself, or its activity, exhibit.

Voyage irregularities

The *Wise Honest*'s route through Indonesia was meant to obscure the cargo's origin; cargo documents prepared for the *Ken Orchid* listed Balikpapan, Indonesia, as the coal's port of loading.⁹ The certificate of origin for the coal found on board the *Wise Honest*, in turn, claimed that the cargo originated in Russia, and a contract mentioned in the forfeiture complaint reportedly included a provision stating that 'the shipowner shall take the ship through one safe port in Russia' and that cargo documents would be prepared once the vessel arrived there, not before.

Tip: Voyage irregularities, including economically unjustifiable detours and loitering, are a red flag requiring further investigation. North Korean vessels are also known to transfer coal

to Russian or Chinese ports, where foreign-flagged vessels then pick it up to deliver it to the ultimate destination, while claiming its origin in those countries.

Falsified cargo documents

Had the Indonesian authorities not intercepted the *Wise Honest* before it could transfer its cargo to the receiving vessel, the *Ken Orchid*, the vessel and its owner would have been drawn into illicit activity carried out by the vessel's charterer. Similarly, the cargo's buyer would have taken delivery of sanctioned North Korean coal (and paid \$3 million to the North Korean regime).

Tip: For sensitive goods and commodities, particularly those restricted by sanctions, do not rely on cargo documentation, and independently verify the cargo's origin.

The cargo's final destination should also be verified, and the case of Trafigura vividly demonstrates why. In October 2017, the *Lighthouse Winmore* conducted a prohibited ship-to-ship transfer of petroleum products with a North Korea-flagged vessel. The ship had been chartered just a month earlier by Oceanic Enterprise Ltd., a Marshall Islands company controlled by a Taiwanese national. The ship was subsequently detained by South Korean authorities and during the investigation Trafigura was identified as the cargo's shipper. As it later transpired (not before the company was forced to issue statements denying its involvement in sanctioned activities) that Trafigura had sold the fuel to a Hong Kong-based trader, Global Commodities Consultants Ltd., on a free-on-board basis. Global Commodities Consultants subsequently sold the oil to Oceanic Enterprise Ltd., the company that chartered the *Lighthouse Winmore*.¹⁰

Tip: At the Panel's recommendation, Trafigura adopted additional

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contractual clauses in its risk management framework, including requiring proof of the cargo's final discharge and a requirement that buyers themselves require continuous AIS transmission.

Risk assessment and continuous monitoring

Sanctions evaders – be it North Korea, Iran, or other actors – rely on effectively the same set of sanctions evasion tactics. These tactics, however, change and get more sophisticated over time, so keeping up to do date with industry sources can go a long way toward mitigating sanctions risks.

It is also worth emphasizing that vessel risk profiles are not constant over time, and should be reviewed periodically after the initial due diligence. One recent example of why this is so important concerns the vessel *Courageous*, the latest target of US civil asset forfeiture. In a pattern that will by now be familiar, in July 2019, the *Courageous* was sold to a new owner, a company registered in China, through a Singaporean broker. Shortly thereafter, the ship switched off its AIS and began making oil deliveries to North Korea, both directly and through ship-to-ship transfers.¹¹ The ship was expelled from Taiwan in February 2020 and detained in Cambodia shortly thereafter.¹² In addition to the civil asset forfeiture complaint, the US government also filed charges

against the Singaporean broker, who appears to have ties to another ship making illicit deliveries to North Korea. (Of note, both vessels had been investigated by the UN North Korea PoE, with details laid out in periodic reports.)

Conclusions

In February 2018, the ship *Wan Heng 11* was detected engaging in a ship-to-ship transfer with a North Korean tanker while under a bareboat charter. When the vessel was deregistered by its flag state as a result of this incident, the owner tried to activate the charterparty's illegal trading clause and recover the vessel – unsuccessfully. The vessel switched off its AIS and shortly thereafter took on the North Korean flag.¹³

This is a good reminder that sanctions risk comes not only from regulators, but also includes a very real possibility of direct asset loss. As such, actors in the maritime space should treat sanctions risk seriously, and adopt a suite of mitigating measures – from institutionalising compliance programmes, conducting comprehensive KYC checks, and supply chain due diligence, to vessel monitoring, contractual clauses, and information-sharing wherever practicable. Detecting sanctions evasion is not an easy task, but appropriate tools make it that much more feasible. **Tip**