Global service
built around you

North

Home: Sanctions Compliance in the Shipping Industry

Articles: Sanctions Compliance in the Shipping Industry

Mike Salthouse, Global Director (Claims) reviews sanctions compliance in the shipping industry following the recent U.S Global Maritime Advisory published in May 2020.

On 14 May 2020 the US issued new guidelines for the marine industry setting out US expectations of the measures that the industry should be taking to ensure that shipowners, insurers and flag states to name but a few adhere to US law.

The Advisory covers the following industry sectors:

- Marine Insurers
- Flag Registry Managers
- Port State Control Authorities
- Shipping Industry Associations
- Commodity Traders, Suppliers and Brokers
- Financial Institutions
- Shipowners, Operators and Charterers
- Classification Societies
- Vessel Captains
- Crewing Companies

This is a truly ambitious document aimed at providing detailed guidance to all sectors of the shipping industry – an industry which Washington for some time, has felt lags behind best compliance practice. The shipping industry accounts for 90% of the world's trade and for many of those involved the publication of the Advisory will require a significant increase in the time and resources spent on compliance. Given that the US has consistently demonstrated a willingness to act against sanctions breakers, no one should be in any doubt of the US commitment to ensuring its sanctions' legislation is complied with.

The publication of the Advisory had been widely trailed and the US Government should be commended for the extensive industry outreach conducted as part of its ambitious programme of activities that aim to improve and consolidate relationships between industry and policy makers in Washington. Nevertheless,

behind that outreach lies an established enforcement agency and whilst the Advisory is expressed to be non-legally binding some parts of the shipping industry will feel uncomfortable about the expectation that non-US nationals adhere to a US Foreign Policy which may be at odds with that of their own country. So while United Nations sanctions against North Korea are universally accepted, US policy towards Iran is not, and the conflicting legislation of the US and EU is an example of where compliance with one set of rules places a company or person at risk from prosecution in one jurisdiction or the another.

US Officials address that conundrum by pointing out that it is only those subject to US jurisdiction that face prosecution, but for those that are not the choice is simple. A non-US business is free to engage with a US sanctions target but if it does it cannot at the same time do business with US companies or persons. That would mean a loss of access to US financial services and more particularly dollar transactions. For most involved in shipping the risks associated with losing access to US markets will far outweigh any short-term advantages derived from doing business with a US sanctions target.

The Advisory makes repeated statements to the effect that the recommendations contained within it are not legally binding and the main body of the guidance tries hard to strike a pragmatic balance between compliance with US law and what is practical recognising the constraints under which the industry operates. However, the Additional Guidance for specific industry sectors contained in Annex 1 are more specific in setting out US expectations and this could give rise to difficulties for reasons that I explore below:

1. Enforcement.

That the US can enforce its laws against non-US persons is not in doubt but the way it does so is worth considering. US enforcement action relies on the dominant position enjoyed by the US dollar. If a business wishes to engage in dollar transactions or to do business with other companies that conduct transactions in US dollars then it is vulnerable to US enforcement action the effect of which is to prevent access to US financial markets.

However, what the US does not have the power to do is to conduct investigations into the conduct of companies that are not domiciled in and do not have a presence in the US. In simple terms OFAC has no power to compel a non-US business to cooperate with an investigation into that business. It therefore occupies the roles of prosecutor, judge and executioner without providing the target company with any formal mechanism by which to defend itself. So, if the threshold for a breach of sanctions by a non-US company is a failure to exercise due diligence the accused company has no right or forum in the US within which to argue that it exercised due diligence to ensure that sanctions were not breached.

This has always been the case for US secondary sanctions but given the detail contained in the guidance, the mechanisms by which an accused non-US company is given the opportunity to demonstrate that it has done its best to comply with the

guidance are far from clear. The concern in industry is that any failure to apply measures in accordance with the published guidance will result in sanctions.

Over compliance is a likely consequence of the Advisory particularly within the heavily regulated financial services sector. That would be unfortunate because at best the disruption to legitimate trade can be disproportionate to the targeted sanctions breaking activity. At its worst it can stigmatize the shipowner or charterer that is simply trying to do its best.

2. Advisory versus Contract.

Another area which is unclear is the extent to which the US now expects the shipping industry to break contractual commitments based on a *suspicion* of sanctions breaking. For example, a vessel may be contracted on a period time charter and be ordered by its time charterer to load a cargo by way of STS from another vessel. Ostensibly this is a lawful order. The shipowner would only have the right to refuse the order if it was unlawful and involved a breach of sanctions. The shipowner may have concerns about the origin or destination of the cargo but at law lack the evidence necessary to refuse to comply with the charterer's order. If in the absence of such evidence the shipowner feels compelled to comply with that order how is the decision to carry out the STS going to be viewed by the US whose enforcement agencies will have no access to the contract terms or indeed the decision making employed by the shipowner in deciding to carry out the charterers order?

3. Against the law.

The Advisory does not address inconsistencies in legislation to which a multinational shipping industry is subject. There are three main areas in which this presents a problem – Competition law, data protection law and International Maritime Conventions such as SOLAS.

i. Competition law.

From the perspective of the US it must be frustrating that a vessel denied coverage from a P&I club or Classification Society can then secure similar services from another club or classification society because information is not shared concerning suspicions of sanctions breaches. But both IACS and the International Group occupy significant market positions within shipping and are heavily regulated by the EU Competition authority and/or domestic anti-competition law. If all 13 clubs in the International Group collaborated to deny cover to a tanker operator, then it would have a profoundly detrimental effect upon that tanker operator's ability to do business. The position would be the same if the tanker was refused access to a classification society that was a member of IACS. Competition law is absolutely clear on this point – namely that to share information based on a suspicion that the operator has engaged in sanctions breaking as opposed to a fact (for example the shipowner is designated) would be an abuse of a dominant market position and expose the club or classification society to very significant fines.

ii. Data Protection Law.

Similarly, businesses – particularly those based in Europe – are obliged to safeguard personal data. The Advisory makes specific recommendations concerning the handling of personal data of shipowners in the annexes relating to Marine Insurers and Classification Societies but UK and EU businesses are required to comply with the General Data Protection Regulation, which restricts the extent and nature of personal data processing to that required by law or necessity. As the financial crime legislation UK and EU businesses are subject to does not mandate the routine collection of personal data about beneficial owners, it is not clear how the requirements of data protection law would be satisfied were insurers and classification societies to hold and share this level of personal details to the extent suggested by the Advisory. The General Data Protection Regulation contains particularly stringent penalties for companies who transgress.

iii. International Convention.

Active monitoring of AIS is a much-repeated theme of the Guidance. And compared to earlier drafts the guidance as published acknowledges that a ship's signals may be lost and / or the system turned off for proper reasons. But consider this. Under SOLAS the Master may cease AIS transmissions in the interests of the safety of the ship, its crew and cargo. However, the publication of the guidance will lead to ship managers pressuring a ship master to keep broadcasting in circumstances where previously it may have been turned off for safety reasons in accordance with SOLAS. It would be unfortunate if a vessel and its crew were tracked and subsequently seized by pirates using AIS to identify potential targets – I am sure Captain Phillips had turned his AIS off in the period before the Maersk Alabama was seized. And if he hadn't – he should have done!

The whole conversation around AIS does not accommodate the inherent problem with its use as a compliance tool; specifically that there are legitimate reasons why it may have been turned off and technical reasons why a signal may not have been received and that being the case it is nigh on impossible to use it without corroborating evidence as a basis for breaking a contract or terminating services such as Class or insurance. One commercial provider of commercial AIS tracking software has observed that data on about 30% of ships is routinely lost and yet there is no suggestion that 30% of the merchant fleet is at any one time engaged in unlawful or underhand trade.

4. Iran.

The Guidance also sets out US expectations in relation to Iran sanctions. This creates something of a dilemma for non-US parties and specifically those subject to EU law. The US is alone in its withdrawal from the Joint Comprehensive Plan of Action and the reinstatement of US secondary sanctions lifted as part of that agreement in 2016. A European service provider or ship operator has since November 2018 been left in the invidious position of breaking either EU or US law when it comes to certain Iran nexus trades. This has caused real compliance difficulties. It is profoundly unsatisfactory that businesses striving to do their best

are left in such a position without guidance or support from either the EU / UK or an acknowledgement of the difficulties faced from the US.

It is perhaps inevitable that a document of the breadth and ambition of the recent Advisory will give rise to questions and inconsistencies. In its current form however it should though be seen for what it is; a genuine attempt on the part of the US to provide guidance as what constitutes best practice in the field of Iranian, Syrian and DPRK sanctions compliance. The US made a genuine effort to reach out to the maritime industry and listened to the concerns expressed over earlier drafts. The guidance, whilst detailed and undoubtedly operationally onerous nevertheless provides real insight into what is expected and any part of the maritime industry which in the past has been prepared to ignore compliance for the sake of the proverbial “quick buck” can now be in no doubt of the standards to which it will be held to account.

Want to know more?

Contact our sanctions team directly at sanctions.advice@nepia.com to discuss any sanctions enquiries in more detail.

CONTRIBUTOR

Mike Salthouse

Global Director (Claims)

Office
+44 191 232 5221

Mobile
+44 771 321 5177

Email
mike.salthouse@nepia.com