A large global financial institution faces a myriad of sanctions risks that vary from one jurisdiction and line of business to another. The risks also evolve as individuals and entities subject to sanctions seek to evade controls and new regulations are put in place to counter their efforts. How can an institution keep up? How can it identify all of the relevant risk factors that create exposure to sanctions?
Moving beyond the FFIEC Manual
The Bank Secrecy Act/Anti-Money Laundering (BSA/AML) Federal Financial Institutions Examination Council (FFIEC) Manual has traditionally been the focal point for guidance in performing a risk assessment for compliance with the Office of Foreign Assets Control (OFAC) sanctions. Indeed, the key reference related to OFAC, “Appendix M: Quantity of Risk Matrix – OFAC Procedures,” remains an important guide as the categories of risk factors addressed, including customer base, products and geography, continue to be relevant and aligned with the way examinations and risk assessments are organized. However, the manual itself was designed as a guide for bank examiners rather than financial institutions, and Appendix M was last updated before the enactment of several of the most significant sanctions measures in force today. To fully identify and assess today's real sanctions risks, global financial institutions must look beyond the FFIEC Manual to sources that are current and relevant to their business profile.

The following four steps outline an approach to leveraging key sources that can help identify sanctions risks.

1. **Understand the relevant sanctions authorities and how they apply.**

   Both US and non-US financial institutions that operate globally must understand the nature of the sanctions risk they face across sanctions programs and how that affects their operations within and outside of the US. This is particularly important for non-US institutions, which are only subject to OFAC jurisdiction with respect to their US presence, employment of US persons and access to the US financial sector. In addition, certain industries, such as shipping, oil, insurance and those dealing in precious metals, have recently been targeted for sanctions through various new authorities. Examples of how an understanding of sanctions authorities may help to identify risks include:

   ▶ **Customer nationality** – identifying the nationality of your customer base in light of US sanctions associated with nationals of sanctioned countries. For instance, while a US financial institution is generally prohibited from conducting business with Cuban nationals outside of the US (i.e., “wherever located”), non-US financial institutions, which are often allowed to facilitate Cuban business in their home jurisdictions and elsewhere, must be aware of the “contagion effect” and be sure to segregate any such business from the US. Similar considerations apply to nationals from other sanctioned countries, such as Iran, Syria and Sudan.

   ▶ **Customers and transactions in certain sectors** – recognizing that sanctions target certain trade with Iran related to oil and precious metals suggests that customers or transactions associated with these sectors may be considered risk factors. This could include customers that are involved in the trading, brokering or transporting of oil, as well as the financial institution’s participation in commodities-trading activities related to oil and precious metals. Commodities trading, in particular, can often present challenges in identifying the involvement of Iranian parties as purchasers, originators or recipients of a product.

2. **Understand current trends of sanctions evasion.**

   Sanctioned parties are constantly seeking new methods to circumvent controls and evade sanctions, making the screening of names alone an insufficient control. The US Treasury, including OFAC and the Financial Crimes Enforcement Network (FinCEN), disseminates a wealth of information that exposes the tactics of sanctions evasion to aid financial institutions in protecting themselves against these activities. This information can be drawn from both advisories and enforcement actions. For example:

   ▶ **FinCEN advisory** – In a June 2010 advisory, FinCEN noted that the sanctioned Islamic Republic of Iran Shipping Lines (IRISL) “has employed deceptive practices to evade scrutiny, including renaming and relagging its vessels and adjusting the information associated with financial transactions to conceal IRISL’s involvement,” and that “the International Maritime Organization (IMO) registration number assigned to each vessel is a unique identifier that cannot be reassigned to another ship and remains with the ship throughout the life of the vessel.” FinCEN further advised that “IMO numbers could provide a useful indication of whether an IRISL vessel is involved in a transaction. The IMO numbers for IRISL vessels previously identified by the US are provided on the Specially Designated Nationals and Blocked Persons List (SDN List) published by OFAC.” As many banks typically screen the names of vessels involved in a transaction, this advisory identified the IMO number as a more reliable data point in identifying sanctioned parties.

   ▶ **OFAC advisory** – In March 2011, OFAC issued an advisory warning of IRISL’s efforts to evade sanctions by fraudulently modifying the number scheme assigned to containers in shipping transactions: “Documents making use of these practices can be used to facilitate IRISL’s shipping business and the financing of transactions involving merchandise shipped on vessels that have been identified as blocked, including through letters of credit and other trade finance facilities.” This suggests that a financial institution involved in trade finance transactions should evaluate the specific information it receives in the associated documentation with a view to identifying fraudulent information that could be used to bypass controls.

   ▶ **OFAC advisory and associated enforcement action** – In January 2013, OFAC issued an advisory to highlight Iran’s use of “third-country exchange houses or trading companies that are acting as money transmitters to process funds transfers through the United States in support of business with Iran,” in an effort to evade sanctions controls. Shortly thereafter, in May 2013, the US Treasury sanctioned Al Hilal Exchange and Al Fida International General Trading, both based in Dubai, for providing services to
Iran’s Bank Mellat. In its action, the Treasury asserted that “Bank Mellat used an account at Al Fida International General Trading to transfer currency to Al Hilal in an attempt to obscure the origin of the funds.” As a result of the advisory and the additional Treasury action, it is evident that customers that operate as exchange houses or trading firms, especially in the UAE, can be reasonably considered a particular risk factor.

3. **Use the OFAC SDN List to understand how your business is uniquely exposed to sanctioned parties.**
   This could be specific to a particular geography or to the activities of a particular customer or customers. For example, a review of the OFAC SDN List for entities located in Singapore shows Iranian front companies involved in shipping activities. This would suggest that shipping activities involving Singapore could be a risk factor for sanctions. In addition, if a significant customer or group of customers located anywhere in the world is involved in shipping-related activities in Singapore, those customers could raise the risk of exposure to potentially sanctionable activities.

4. **Review academic research, press reporting and trade statistics to identify information about jurisdictional risks.**
   Political and economic relationships with sanctioned countries and analysis of trade patterns, economic activity and the presence of sanctioned entities offer the possibility to distinguish between different characteristics of risk. For example, the same business profile in Turkey and Japan will pose different sanctions risks:
   - **Turkey** – Following US action to sanction the provision of gold to Iran, press reporting indicated a steep rise in gold exports from Turkey to Iran. As neighbors, Turkey and Iran maintain a long-standing and robust cultural and trading relationship.
   - **Japan** – Japan’s relationship with Iran and exposure to sanctioned entities is much different from Turkey’s. Although Japan is an importer of Iranian oil, it does not share a border or as deep a cultural and trade relationship with Iran. Rather, Japan faces risks from sanctioned parties seeking to access the yen and from organized crime groups that are subject to sanctions. The United Nations Office on Drugs and Crime issued a report in April 2013 chronicling transnational organized crime in East Asia, and in its first use of an Executive Order targeting transnational organized crime, the US Treasury in February 2012 sanctioned elements of the Japanese Yakuza crime family for its “involvement in serious criminal activities, including weapons trafficking, prostitution, drug trafficking, fraud and money laundering.”

**Conclusion**

In many ways, economic sanctions have become the tool of choice for the United States Government and its allies in dealing with threats to national security. As this landscape evolves, current sanctions programs will continue to change, often broadening in scope, while new sanctions programs are likely to emerge as well. The only constant is that sanctions targets will continue seeking to evade controls. To fully understand these risks, financial institutions must look to sources of information that offer current and relevant intelligence about the real risks facing today’s financial system. Identifying these risks will not only bolster confidence in meeting regulatory expectations for sanctions compliance but will also offer valuable insight into the sanctions risk profile of the business.
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