LLOYD'S

Market Bulletin

Ref: Y5358

Title	**Marine sanctions guidance – Enhanced Due Diligence measures**
Purpose	This guidance is to be read in conjunction with Market Bulletin Y5246 and includes new recommendations for enhanced due diligence measures in relation to marine cargo and hull exposures with certain risk profiles.
Type	Event
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Deadline	
Related links	Market Bulletin Y5246 North Korean and other sanctions evasion tactics Guidance to Address Illicit Shipping and Sanctions Evasion Practices HM Treasury's Office of Financial Sanctions Implementation (OFSI)'s – 'Maritime Guidance'
Date	10 December 2021

Background

In April 2019, Lloyd's issued Market Bulletin Y5246 North Korean and other sanctions evasion tactics which highlighted marine-related sanctions evasions tactics, enhanced regulatory scrutiny on the insurance sector, and a risk-based approach to minimise inadvertent exposure to sanctionable activity. This Market Bulletin is to be read in conjunction with Y5246 and provides updated guidance to the market following the publication of further UK and US guidance on measures which may contribute to countering illicit shipping and sanctions evasion. This Market Bulletin is therefore relevant to managing agents and brokers involved in marine hull and cargo risks.

In May 2020, the US Department of State, the US Department of the Treasury's Office of Foreign Assets Control (OFAC), and the US Coast Guard issued Guidance to Address Illicit Shipping and Sanctions Evasion Practices. This Global Maritime Sanctions Advisory provided guidance to a range of marine-related sectors including ship owners, managers, operators, brokers, flag registries, port operators, shipping companies, freight forwarders, and insurance companies.

On July 2020, HM Treasury's Office of Financial Sanctions Implementation (OFSI) issued 'Maritime Guidance' (subsequently updated in December 2020) to provide sanctions compliance guidance for entities and individuals operating within the maritime shipping sector, including the insurance industry. The Maritime Guidance provides information on sanctions evasion practices, and due diligence measures which should be considered to mitigate the risk of any sanctions breach.

Lloyd's has collaborated with the company market / Lloyd's market managing agents and brokers, in conjunction with the Lloyd's Market Association (LMA) and the International Underwriting Association (IUA) to consider both UK and US regulatory expectations in the drafting of this guidance.

This Market Bulletin comprises the following;

- Updated risk factors for underwriters and compliance personnel to be aware of;
- Updated due diligence procedures; and
- Revised enhanced due diligence (EDD) measures, and where appropriate, suggested controls.

Updated risk factors for potential illicit shipping practices

Further to the risk factors outlined in Y5246, UK and US guidance highlighted several additional practices that have been connected to illicit or suspicious shipping activities (red flags). While these practices may not in themselves be breaches of sanctions regulations, they may raise suspicion of underlying illicit activity which does breach sanctions. Such red flags include, but are not limited to;

- **ship-to-ship transfers (STS)** – STS are a legitimate practice of transferring cargo between vessels positioned alongside each other at sea (instead of at port) but has been used to conceal the origin and nature of cargo, and facilitate the illicit transfer of goods to evade sanctions;

- **intentional disabling or manipulation of Automatic Identification Systems (AIS)** – under the International Convention for the Safety of Life at Sea (SOLAS) certain classes of vessels are required to continuously operate their vessel AIS to ensure the transmission of identification and navigational data and the avoidance of collisions. There are legitimate reasons for a vessel's AIS to be turned off or for a transmission not to be received. However, UK and US guidance notes that vessel AIS has also been intentionally disabled to obscure a vessel's whereabouts when conducting illicit trade;

- **cyber-attacks** – used to illegally force the transfer of funds from financial institutions and cryptocurrency exchanges to circumvent financial sanctions;

- **payment via crypto assets** – use of crypto assets for payments within the maritime sphere to avoid detection. Note that the UK guidance reminds that crypto assets are included in the statutory definition of “funds” and “economic resources” and are therefore caught by UK financial sanctions restrictions;

- **use of front or shell companies** – disguising the ultimate destination of goods, funds or services or facilitating illicit shipping practices;

- **falsified documents** – a common tactic for sanctions circumvention is the falsifying of documentation associated with maritime transactions such as bills of lading, and invoices and insurance paperwork. This tactic aims to obscure the origin of a vessel, its goods, its destination or even confirm the legitimacy of the vessel itself.

Due diligence procedures

In line with UK and US guidance, underwriters and compliance personnel are reminded that consideration should be given to EDD measures in cases that are assessed as higher risk.

Red flags – when is EDD triggered?

Where high-risk factors exist, brokers should, to the best of their ability, ensure that a minimum level of due diligence information is provided to underwriters in sufficient time to enable them to consider it and raise further queries. Brokers remain well placed to obtain sufficient placement information to enable appropriate sanctions checks against clients and insurance beneficiaries when cover is issued. [1]

To assist the market in identifying higher risk marine exposure(s), Lloyd’s has compiled a non-exhaustive list of risk factors. Whilst these risk factors are not themselves illegal or prohibited, they have been present in previous cases of sanctionable activity. It is for managing agents and brokers to determine what combination of high-risk factors would trigger EDD measures. Lloyd’s suggests that the presence of two or more risk factors (arising in separate risk categories), should raise a red flag that triggers EDD procedures. If EDD measures do not mitigate the level of perceived risk, consideration should be given as to whether it is prudent to proceed with the provision of cover.

High Risk Factors.xlsx

EDD measures

Where the existence of high-risk triggers has identified a need for EDD, managing agents and brokers are encouraged to seek a detailed explanation of contractual arrangements which could give rise to increased sanctions risks. At a minimum, Lloyd’s recommends that managing agents and brokers to seek to obtain a minimum level of key information from their insured(s). To this end, Lloyd’s has devised two EDD questionnaires for use, one for marine

[1] As outlined in UK Treasury’s Office of Financial Sanctions Implementation (OFSI) Guidance (March 2018)

hull risks and another for marine cargo risks. These are a minimum set of questions (which can be expanded on by managing agents and/or brokers), with some information fields marked as “required” to highlight them as particularly important to obtaining a comprehensive understanding of the risk.

EDD
questionnaire.xlsx

The hull questionnaire includes questions relating to the insured and any counterparties and specific questions on the insured vessel(s), including IMO numbers and the flag of the vessel. The cargo questionnaire also includes questions relating to the insured and any counterparties and asks a series of supply chain analysis questions to seek a clearer understanding of the risk profile.

Given the nature of marine business, it may not be feasible to use the EDD questionnaires in all scenarios, or obtain the information to complete all fields in the questionnaire. This could be the case in quota share reinsurance where the reinsurer will not see granular detail of underlying insured vessels, and/or vessel information such as the load and discharge ports, agents, consignor/ consignees, and end users. However, it is expected that managing agents and brokers will use best efforts to capture the information in the relevant questionnaire.

Brokers are in the best position to request that the relevant EDD questionnaire be completed by the insured. Once completed, the broker should circulate the responses to all subscribing managing agents for their own screening and assessment of the risk. It is not expected that the completion of the questionnaire will be a mandatory pre-requisite to the binding of risk, however in the absence of a completed questionnaire, managing agents should document how they gained sufficient comfort to proceed with a risk.

Other controls

The use of these questionnaires is one of a range of EDD measures that could be deployed. Market Bulletin Y5246 outlines other risk mitigation measures such as the use of sanctions clauses or, where warranted, deploying technology solutions such as the use of commercial tracking/ provision of intelligence to support EDD, screening and ongoing monitoring.

Use of sanctions clauses

The market is reminded that while the inclusion of sanctions limitation and exclusion clauses can provide (re)insurers with a degree of legal protection if illicit activity is detected post-bind, an adequate sanctions clause may serve to suspend liability but might not extinguish liability. As such, the use of such clauses should not be considered as a substitute for the due diligence and pre-bind screening processes detailed in this guidance. Similarly, a direct insurer may seek, as a prudent measure, to introduce contractual clauses that aim to restrict higher risk activity (such as territorial exclusions) or promote continuous AIS broadcast (promoting compliance with the international convention on SOLAS). However, this should be considered as part of the managing agent's risk-based and holistic due diligence and screening programme. See below for more detail on AIS-related clauses.

Use of AIS-related clauses

In January 2021, in response to the aforementioned UK and US regulatory attention on the maritime industry, the LMA/ IUA Joint Hull Committee (JHC) released JH2021/008 AIS Operation Clause. In an associated Circular, the JHC noted that the AIS Operation Clause can be used by marine underwriters to reinforce adherence to SOLAS and give underwriters the means to require the production of AIS records. The intention is that this new clause can "augment the due diligence undertaken in risk selection and would complement the sanctions clause in common use".

For the clause wording and associated Circular, visit the LMA website.

For further information

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