

# Four Things We Learned from OFAC's Recent SDN Designations

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## Overview

Recent actions taken by the US Office of Foreign Assets Control (OFAC) in imposing, then lifting, sanctions on major multinational companies provide important new lessons for their counterparties.

Take, for example, OFAC's January 31, 2020 lifting of sanctions on China-based COSCO Shipping Tanker (Dalian) Co., Ltd. (COSCO Dalian), five affiliates, and one individual, previously named as Specially Designated Nationals (SDNs) in September 2019 for knowingly engaging in a significant transaction for the transport of oil from Iran.

COSCO Dalian, a subsidiary of China Ocean Shipping Company (COSCO), the world's third-largest shipping company, is just one of several major names designated by OFAC as SDNs over the past two years for running afoul of US foreign policy goals. Others include Rosneft Trading S.A. (Rosneft Trading), which was designated in February 2020. They are unlikely to be the last.

Historically, companies placed on OFAC's List of SDNs and Blocked Persons (the SDN List) became instant commercial pariahs. Yet, from our current vantage point in Asia-Pacific, we have observed a shift, with more companies taking a "wait-and-see" approach towards newly sanctioned counterparties, especially if those counterparties are major multinational companies.

Why the change? Three possibilities come to mind. First, it is commercially and politically difficult for companies to simply walk away from large, government-linked or economically important counterparties, even if they are on the SDN List. Second, more non-US companies have implemented sophisticated, risk-based compliance programs for confidently managing OFAC risks. Third, OFAC has shown a willingness to limit or remove sanctions after a relatively short period of time, as in the case of COSCO Dalian and the general licenses for various large, commercial and state-owned entities designated in recent years.

With the possibility of future sanctions in mind, below we provide four big-picture lessons from OFAC's recent SDN designations.

### **Lesson 1: There's no such thing as "too big to sanction"**

According to the US Department of State, COSCO Dalian knowingly engaged in a significant transaction for the transport of oil from Iran, activity which was sanctionable under Executive Order 13846 following the expiration of China's Significant Reduction Exception (SRE) on May 2, 2019. In addition to COSCO Dalian, OFAC designated a second COSCO subsidiary, COSCO Shipping Tanker (Dalian) Seaman & Ship Management Co, Ltd. (COSCO Seaman), four of the companies' affiliates, and five executives as SDNs pursuant to Executive Order 13846, for taking part in the sanctionable transactions. While OFAC clarified, in an FAQ, that the sanctions did not affect the companies' parent, COSCO, the designations caused immediate disruptions to global shipping markets, leading to a significant increase in some rates.

OFAC's COSCO sanctions were reminiscent of its April 6, 2018 designations of several prominent Russian individuals and companies following the October 2017 adoption of the US Countering America's Adversaries Through Sanctions Act (CAATSA). See our International Law Advisory on the subject here.

More recently, on February 18, 2020, OFAC designated Geneva-based Rosneft Trading, a subsidiary of the Russian energy giant, as an SDN pursuant to Executive Order 13850 for operating in the oil sector of Venezuela. While the Rosneft Trading designation has not had a major impact on world oil prices, OFAC's decision once again illustrates the agency is not afraid to sanction major players to promote US foreign policy objectives, such as the downfall of the Nicolás Maduro government in Venezuela.

OFAC's targeted designation of COSCO and Rosneft subsidiaries, rather than the parent companies, succeeded in generating headlines while avoiding some of the disruptions associated with across-the-board sanctions designations. While the unintended consequences may be fewer, the strategy nevertheless adds to the challenge of companies that must sort through name-screening alerts to separate sanctioned entities from their similarly named but un-sanctioned affiliates.

## **Lesson 2: Good things come to those who wait (sometimes)**

Following months of behind-the-scenes negotiations, on January 31, 2020, OFAC removed COSCO Dalian and several related parties from the SDN List, unblocking the companies' property frozen since September 25, 2019. COSCO Seaman remains on the SDN List as of March 2020. The delistings were a welcome reprieve for the companies, as well as their customers, suppliers, lenders, joint venture partners, and others whose business with the companies had been impacted by the designations.

In these and other similar cases in recent years, the companies' banks and other counterparties faced difficult decisions about whether to walk away from their commercial relationships. Although some chose to simply close accounts or terminate existing or prospective contracts, others stuck by the companies, carefully examining their activities to ensure compliance with applicable US sanctions, while continuing to perform legally permissible transactions that did not fall within US enforcement jurisdiction. Their ability to do so was enhanced by earlier investments made in building strong compliance programs and advice from qualified external legal counsel. Ultimately, these companies were best positioned to minimize losses from the sanctions and reap the commercial benefits upon their termination.

## **Lesson 3: Advocacy can make a difference**

For SDN companies seeking removal from the SDN List, having the right legal and communications support is critical. OFAC has previously stated that it would consider removing persons from the SDN List under some circumstances because the "ultimate goal of sanctions is not to punish, but to bring about a positive change in behavior." While there is little public guidance for companies hoping to be removed from the SDN List, OFAC advises that a sanctioned person (acting alone or with the assistance of counsel) "may submit arguments or evidence that the person believes establishes that insufficient basis exists for the designation." Additionally, the person "may propose remedial steps on the person's part, such as corporate reorganization, resignation of persons from positions in a blocked entity, or similar steps, which the person believes would negate the basis for designation."

In the case of COSCO Dalian, the Chinese government may have sought delisting as part of ongoing US trade negotiations. While diplomatic considerations may play a role in delisting, the decision ultimately comes down to OFAC's view of the facts underlying the SDN designation and, taking into consideration the views of other relevant agencies, whether the target's commitments are sufficient to assuage US foreign policy or national security concerns.

Persons who intend to file an application for delisting must ensure that any disclosure made to the US government is not only accurate and complete, but also must typically demonstrate one or more of the following: (i) the US government's designation was based on incorrect factual information, (ii) US policy has changed in a way that no longer warrants designation, or, most typically, (iii) the target has changed its behavior in a way that is consistent with US policy objectives. The latter includes, among other things, ceasing any sanctionable activity. However, even a successful application for removal from the SDN List can take many months.

Meanwhile, SDN companies must ensure that stakeholders such as shareholders, customers, suppliers, lenders, and other are adequately informed of their strategy and prospects through public statements, media, and other forms of corporate communications. Proactive engagement can help in preserving important commercial relationships and assuring partners of a company's intention to comply with US sanctions in the interest of everyone concerned. Moreover, companies may enlist important stakeholders – particularly US-based suppliers – to help advocate to the US government about the impact of sanctions, such as the number of US jobs at stake. This strategy applies also to companies on other lists such as the Entity List administered by the Department of Commerce's Bureau of Industry and Security (BIS).

## **Lesson 4: It pays to be practical and proactive**

While every company is entitled to make its own risk-based decisions about how to deal with a sanctioned counterparty, the growing variety and prevalence of US sanctions makes it harder for non-US companies, especially in regions such as the Asia-Pacific and Middle East, to avoid such business altogether in perpetuity.

Companies operating in higher risk regions and sectors (e.g., shipping, finance, and energy) may want to think ahead to understand how US sanctions apply (and do not apply) to their businesses, as well as the steps that can be taken to mitigate risks. These steps include implementing a sanctions compliance program with elements such as name screening, ongoing customer due diligence, escalation and approval procedures, periodic employee training, and recordkeeping. Additionally, non-US companies may want to adopt a recusal policy to ensure their US-person employees are not involved, directly or indirectly, in unlicensed transactions with SDNs or other sanctioned counterparties.

*For more information about these issues and guidance on how to implement a risk-based sanctions compliance program for your company's Asia-Pacific operations, contact Steptoe Hong Kong.*

## Practices

### **Economic Sanctions**

### **Export Controls**