

Detecting and Preventing Sanctions Evasion and Circumvention in Trade

Practical Guidance for Economic Operators

The EU has imposed unprecedented restrictive measures on Russia that cover more than 50 percent of the EU trade with Russia. The effectiveness of EU sanctions on trade is eroded and reduced by sanctions evasion and circumvention. Russian and Russia-related EU and third country economic operators have invented numerous ways to evade and circumvent EU sanctions. While the main focus is on individuals and entities that facilitate sanctions evasion intentionally and knowingly, it is equally important to note that facilitation of sanctions evasion may equally happen due to lack of information and adequate training both in the private and public sectors.

Sanctions Regulations are directly applicable law in the European Union Member States. Sanctions circumvention is prohibited by the Regulations and circumvention is punishable criminal activity according to Member States legislation. EU's sectoral sanctions and individual sanctions¹ against Russia should be implemented in parallel. This means, for example, that if an export operation is not prohibited by the sectoral sanctions, the company should still implement individual sanctions and make sure that the exported goods or technologies do not benefit the sanctioned parties or entities under their ownership or control. The applicable EU Regulations lay down on EU operators (and operators conducting business in the EU) the obligation to freeze assets of the sanctioned parties and the prohibition to make funds and economic resources directly or indirectly available for them.

All economic operators should establish, implement and regularly update internal guidelines on compliance with EU sanctions (due diligence). The guidelines should take into account company's business model, the geographical areas and characteristics of the business as well as the related risk assessment of customers and personnel. Company's informed business decisions should be based on the best available information concerning sanctions' risks and sufficient due diligence procedures, including Know Your Customer (KYC) procedure. Company should document those accordingly.

There is a need for practical instructions on detection and prevention of circumvention of sanctions. This document has been drafted for this purpose. The aim of the guidance is to support companies in their responsible business. The document presents due diligence recommendations and red-flags for detecting potential sanctions evasion and circumvention by so far identified in co-operation of European authorities. The document suggests practical ways to investigate and detect sanctions evasion and circumvention. Any information on possible or detected sanctions evasion or circumvention should be reported to the National Competent Authorities in the EU Member States. This guidance is a living document and will be updated as soon as the need has been identified.

This guidance is not obligatory by nature. This is a memorandum drawn up at expert level in the preparation of which the instructions of various EU and Member States authorities and their findings on the circumvention of sanctions have been used. It was prepared by national competent authorities responsible for coordination of sanctions implementation of EU frontier states – Estonia, Finland, Latvia, Lithuania and Poland.

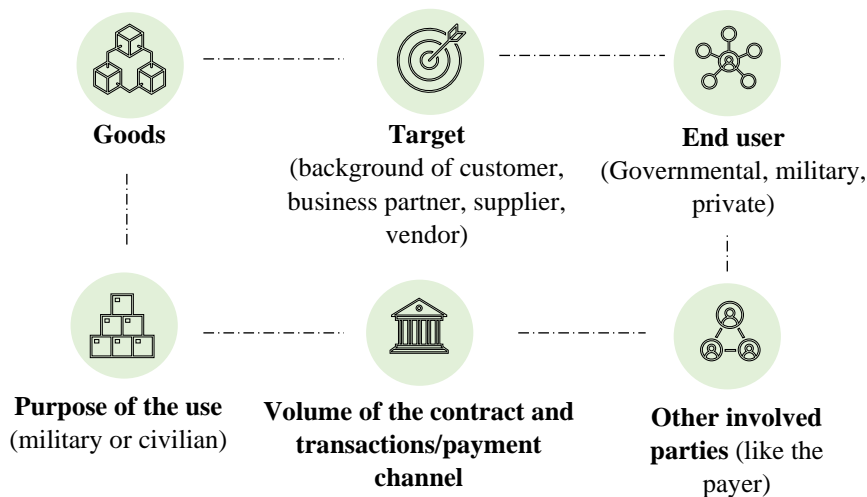
¹ The individual sanctions target people responsible for supporting, financing or implementing actions which undermine the territorial integrity, sovereignty and independence of Ukraine or who benefit from these actions. The individual sanctions can also target persons or entities circumventing EU sanctions or facilitating circumvention of sanctions.

This Paper consists of the following parts:

1. What is risk assessment and which factors should it take into account?
2. Issues to be considered in the company's KYC Procedure.
3. Red-flags in Russia or third country related business operations.
4. Practical guidance to European companies on due diligence when estimating the risk on sanctions evasion and circumvention.
5. Annex I
 1. How to determine ownership and control?
 2. What is the "ultimate beneficial owner" and why does it matter?

1. What is risk assessment and which factors should it take into account?

Appropriate **risk-based approach** will assist companies to manage the potential threats and vulnerabilities in their operating environment in relation to sanctions. A risk assessment (for more information please refer, for example, to [Q&A due diligence on restrictive measures](#)) is a process to identify potential risks by evaluating the probability of the occurrence of an event and the potential damage caused by the event. The scope and extent of the assessment could take into account the following points:



2. Issues to be considered in the company's KYC Procedure

Analysis of possible sanctions evasion or circumvention risks should be part of company's usual KYC. The following main questions should be taken into account when performing the KYC Procedure:

- Is your product/service subject to sanctions?
- Is your business partner on the sanctions list, or owned or controlled by a sanctioned party?
- Is your business partner connected to entities related to e.g., Russian defense sector or entities suspected or known for trading sanctioned goods and technologies to Russia?
- Is a shareholder, any member of governing body of your business partner (management board, supervisory board or similar) or any C-level employee (e.g., Chief Executive Officer (CEO), Chief Financial Officer) linked to entities related to e.g. Russian high-ranking officials / politically exposed persons (PEPs), Russian defense sector or entities suspected or known for trading sanctioned goods and technologies to Russia?
- What is the planned transaction and is there a risk for circumvention of sanctions? Does the case have any of the characteristics of the red-flag situations (see the detailed list of possible red-flags below)?
- Who is the end user? Can the end user certificate be provided? Please be aware of the possibility that you might be provided with a fake end user certificate.
- Who is the payer? What bank will the payer use?
- Does your business contract include sanctions circumvention and responsibility clause?
- Have you established your company internal processes for the KYC including documenting the KYC process in a written format?

3. Red-flags in Russia or third country related business operations

The following red-flags have been collected from the information and observations of the various authorities of the EU and Member States regarding the circumvention of sanctions:

1. European company's **export is redirected to third countries**, the economic operators of which² are known to help Russian economic actors to import sanctioned goods and technologies, and there are sufficient grounds to believe that **the final destination of the goods and technologies is Russia**;
2. Special attention should be paid to domestic/European companies
 - a. that have had long term trade with Russia.
 - b. whose business refers to Russian trade.
 - c. that have only recently changed their operations or opened up activities abroad, for example to third countries.
 - d. whose activities (exports, imports and financial transactions) differ significantly from the previous ones.
3. **New business partner in a third country**;
4. Business partner had been **recently established** or has merged with a sanctioned entity or an entity linked to sanctioned entities or persons;
5. Business partner **shares address** with several dozens of different companies (e.g., it is likely a shelf company);
6. CEO/manager is **never available for discussions**, i.e., all communications go via a regular employee or a representative who seems to have a general Power of Attorney (PoA);
7. **Changes in ownership structure** (the company will change ownership to a non-sanctioned entity, especially when the transfer of ownership is linked in time to the sanction status)
8. **Complexity** of ownership or management arrangements and use of **undercover companies** (including the use of family members, complex business arrangements, transfers of shares, change of company names, use of well-known offshore locations);
9. **Location** of Russian companies **in conjunction with sanctioned entities** and participation in trade;
10. Business partner is a company focusing on **freight transport** (transport companies have been used to circumvent sanctions) or agency/mediator/broker of goods or services;
11. Payments and communication related red-flags:
 - a. **Unusual payment methods** or currency.
 - b. **Multiple payment arrangements**.

² Please see, for example, the US FINCEN and BIS notice on attempts to circumvent sanctions in the context of export controls ([FinCEN and Bis Joint Alert](#))

- c. **Transfers** are **connected to sanctioned** individuals or entities (e.g., payments on behalf of a sanctioned entity).
 - d. Payments are made to or come from **third parties**.
 - e. Cross border movement of money.
 - f. **Russian or Belarussian domains** for electronic communications.
 - g. **Russian or Belarussian telecoms** operators' services (identifiable by area code).
 - h. Preference to **encrypted messaging platforms** for communications, e.g., WhatsApp, Signal etc. with **no apparent reason**.
12. Other signs e.g., entering into a trade agreement with a **third party**, use of **family members**).
13. Product and service related red-flags:
- a. See the lists published by the European Commission on [High Priority Battlefield Items](#) and [Economically Critical Goods](#).
 - b. Crypto services³:
 - i. A customer's transactions are initiated from or sent to Internet Protocol (IP) addresses in Russia, Belarus or FATF-identified jurisdictions with AML/CFT deficiencies.
 - ii. A customer's transactions are connected to **virtual currency addresses** linked to **sanctioned** subjects.
 - iii. A transaction has direct or indirect transactional exposure to **virtual currency exchanges** or services located in **Russia**.
 - iv. A customer initiates a transfer of funds involving **crypto mixing service**.
 - c. Use of **valuable assets**.
 - d. Covering the origin of merchandise:
 - i. Product code **alteration**.
14. Sector related red-flags:
- a. Transport sector, logistics:
 - i. The customer purchasing the goods is **recently registered**.
 - ii. The activity of the customer **does not correspond** to the category of the purchased product.
 - iii. The goods are transported by **illogical route** (longer or unusual route).
 - iv. The customer before 24 February 2022 had business relationships with individuals or entities now **designated** and/or had dealings that involve products that are currently subject to **export restrictions**.
 - v. The customer provides **incomplete information** about the end-user and/or end-use of the product, when asked avoids providing additional information.
 - vi. The description of the goods on the trade/financial documentation is **vague and misleading**.
 - b. Legal and tax advisory companies – possible facilitators of circumvention of sanctions. Please note that legal consultations on compliance are often needed but there might be a short distance from legal consultations on compliance with sanctions to assistance in circumvention of sanctions.
 - c. Energy, aviation, electronics, other advanced technology sectors – please pay attention to transportation companies and transit ports as well as to products that are subject to direct risk to be used for military purposes in Russia.

³ For more red-flags on crypto services refer to: [FinCEN Alert, FIN-2022-Alert001, March 7, 2022, Special Bulletin on Russia-linked money laundering activities \(canada.ca\)](#)

15. **Typical red-flags for money laundering.** *(please see the [List of criteria for identifying money laundering and suspicious transactions or transactions](#)).*

4. Practical guidance to European companies on due diligence when estimating the risk on sanctions evasion and circumvention.

The Commission's Q&A due diligence on restrictive measures for EU businesses dealing with Iran and the findings of various authorities on the circumvention of sanctions have been used in drawing up this section.⁴

1. Ensure you collect at least the following basic level information from your customer:

- a. Full name of the entity.
- b. Legal form (listed, limited, private joint stock etc.).
- c. Registration ID.
- d. Private or state-owned.
- e. Key contact, address, phone, and homepage URL.
- f. Management full names, date and place of birth, ID Number, PEP status.
- g. Shareholder full names and number of shares, date and place of birth, ID Number, Politically Exposed Person (PEP) status.
- h. Ultimate beneficial owner (UBO, please see Annex I for further information).
- i. Ties of management and shareholders to PEPs and sanctioned subjects.
- j. Activities, products.

2. Perform sanctions and open-source checks.

a. Sanctions check:

- i. Check the sanction status of your product or service.
- ii. Check your business partner against sanctions. Search entire company, shareholder and management in the EU Consolidated: Financial Sanctions List and other relevant sanctions list (e.g., US SDN List).

Note that a company should perform sanctions screening in order to ensure compliance with the applicable sanctions.

b. Open-source intelligence: search company's website, news, internet. Media databases and general media should be consulted in order to detect information related to issues such as:

- i. Association with terrorist financing or terrorist activities.
- ii. Links to organized crime or arms trafficking.
- iii. Money laundering.
- iv. Regulatory investigations and material litigation.
- v. Allegations of involvement in bribery and corruption; and/or
- vi. Regulatory investigations or sanctions.

3. Check whether you really know your business partner and the destination of the goods and technologies by answering the following questions:

- a. Do you know your current and future business partners (KYC compliance), their background and chains of ownership, and control and management?

⁴ https://finance.ec.europa.eu/system/files/2020-01/faqs-restrictive-measures-iran_en.pdf

Please see Annex I for further information on ownership and control.

- b. Does your customer/business partner operate through a chain? Is it complicated to track the chain of ownership until the true beneficial owner?
- c. Do you know their business and possible changes in the business profile? Does the partner have connections to PEPs or sanctioned persons or entities, or had?
- d. In the case of a new business partner, what is the reason for the new business relation?
- e. Does your new business partner have a physical residence and a public-facing website?
- f. Is the customer's line of business in line with ordered/provided goods and technology?
- g. How credible is the final use of the exported goods or technologies in the light of the business profile and company's projects? Can the company provide enough documentation to prove the final use?
- h. Where have been the products/technology that your business partner provides/sell sourced?
- i. How are the goods/technology in reference transported? What routes are going to be used?
- j. Did your customer/business partner provide written documentation on the company background and the business case?
- k. Does your customer trade in goods/technology that are subject to export/import restrictions?
- l. Has the volume of goods ordered by the customer increased recently in a way that does not match their known/usual end-user needs/business?
- m. Is the final end-use of goods/technology that are exported to third countries a logistics warehouse?

4. Use official sources to verify collected information:

- a. Official Registers of Companies in the Member States and in third countries.
- b. UBO registers (if applicable).
- c. Other applicable registers (land registry, tax registry, registry for public procurement etc.).

5. Use your networks to source additional information or share the information (if needed):

1. Ask for additional information from your chambers of commerce, EU business associations and EU Member State business associations abroad.
2. Make use of the experience of the other companies on the market (if applicable).

6. Document background checks and investigation:

1. Document the process:
 - a. Sanctions screening.
 - b. Adverse media screening.
 - c. Communication with the customer/business partner on the case.
 - d. Inquiries to different parties.
2. Document the information received in the process and the facts that you are basing your business decision on.

7. Inform the authorities on the sanctions evasion and circumvention cases:

- a. Inform your national competent authority (please see the list on the webpage <http://urm.lt/default/en/foreign-policy/lithuania-in-the-region-and-the-world/lithuanias-security-policy/sanctions>) on the attempts and detected cases sanctions evasion and circumvention (or the suspected efforts to do that) detected by you.
- b. You can also inform about evasion or circumvention of sanctions by using [EU Whistleblower Tool](#).

ANNEX I

1. How to determine ownership and control?

For an EU operator, it is not always evident who has direct or indirect control over its business partner⁵. However, EU operators **must ensure** that they do not make economic resources available (directly or indirectly) to a person or entity who is subject to EU restrictive measures by dealing with an entity, which is controlled or owned by such a person or entity. Additionally, funds and economic resources belonging to, owned, held or controlled by a person or entity who is subject to EU restrictive measures shall be frozen.

The Council of the European Union has given guidance on the interpretation of ownership and control in the *EU Best Practices for the effective implementation of restrictive measures* (hereafter EU Best Practices).⁶ Furthermore, the Commission has published guidance and extensive FAQs (over 500) covering a broad range of topics and continues to update them, in order to assist stakeholders on how to apply the sanctions packages.⁷

Ownership

In accordance with paragraph 62 of the EU best practices, *the criterion to be taken into account when assessing whether a legal person or entity is owned by another person or entity is the possession of more than 50% of the proprietary rights of an entity or having majority interest in it. If this criterion is satisfied, it is considered that the legal person or entity is owned by another person or entity.*

The Commission has given guidance in the FAQ's on how to take aggregate ownership into consideration:

8. Aggregate ownership: If two or more listed persons are each minority shareholders of a non-listed entity, but their aggregate ownership amounts to more than 50% of that entity, should that entity be considered as owned by listed persons?

Last update: 8 April 2022

One should take into account the aggregated ownership of the entity. For example, if one listed person owns 30% of the entity and another listed person owns 25% of the entity, the entity should be considered as owned by listed persons.⁸

The Commission has also given guidance on how to take into consideration changes in the ownership and organizational structures:

5. If, before the listing took effect, the assets of a listed person were transferred to a non-listed third person (e.g. a family member), do the assets still need to be frozen?

Last update: 8 April 2022

Article 2(1) of Council Regulation (EU) No 269/2014 does not apply retroactively. However, it does require the freezing of all assets currently belonging to, or held, owned or controlled by listed persons. If, at the time of the assessment, there are reasonable grounds to believe that certain assets "belong to" or are "controlled by" the listed person, even if they are nominally owned by someone else, then these assets must be frozen under Article 2(1). It does not matter when the assets were transferred.

⁵ [Q&A due diligence on restrictive measures for eu businesses dealing with Iran \(europa.eu\)](https://data.consilium.europa.eu/doc/document/ST-10572-2022-INIT/en/pdf).

⁶ <https://data.consilium.europa.eu/doc/document/ST-10572-2022-INIT/en/pdf>.

⁷ https://finance.ec.europa.eu/eu-and-world/sanctions-restrictive-measures/sanctions-adopted-following-russias-military-aggression-against-ukraine/frequently-asked-questions-sanctions-against-russia_en.

⁸ https://finance.ec.europa.eu/system/files/2023-05/faqs-sanctions-russia-assets-freezes_en.pdf, question 8.

Regarding the assessment, the criteria exemplified in the past by the Commission in the context of ‘control’ were non-exhaustive. In situations involving third persons (and possible family ties), other elements could also be taken into account, such as:

- the closeness of business and family ties between the listed person and the third person;
- the professional independence of the third person now owning the assets;
- previous gifts given to the third person and how they compare to the transaction in question;
- the frequency/regularity of previous gifts to the third person;
- the content of formal agreements between the listed person and the third person;
- the nature of the assets (e.g. whether these are shares in a company owned or controlled by the listed person).⁹

Control

The EU Best Practices states the following regarding the control criteria:

63. The criteria to be taken into account when assessing whether a legal person or entity is controlled by another person or entity, alone or pursuant to an agreement with another shareholder or other third party, could include, inter alia:

(a) having the right or exercising the power to appoint or remove a majority of the members of the administrative, management or supervisory body of such legal person or entity;

(b) having appointed solely as a result of the exercise of one's voting rights a majority of the members of the administrative, management or supervisory bodies of a legal person or entity who have held office during the present and previous financial year;

(c) controlling alone, pursuant to an agreement with other shareholders in or members of a legal person or entity, a majority of shareholders' or members' voting rights in that legal person or entity;

(d) having the right to exercise a dominant influence over a legal person or entity, pursuant to an agreement entered into with that legal person or entity, or to a provision in its Memorandum or Articles of Association, where the law governing that legal person or entity permits its being subject to such agreement or provision;

(e) having the power to exercise the right to exercise a dominant influence referred to in point (d), without being the holder of that right²¹;

(f) having the right to use all or part of the assets of a legal person or entity;

(g) managing the business of a legal person or entity on a unified basis, while publishing consolidated accounts;

(h) sharing jointly and severally the financial liabilities of a legal person or entity, or guaranteeing them.

64. If any of these criteria are satisfied, it is considered that the legal person or entity is controlled by another person or entity, unless the contrary can be established on a case by case basis.

65. The fulfilment of the above criteria of ownership or control may be refuted on a case by case basis.

⁹ https://finance.ec.europa.eu/system/files/2023-05/faqs-sanctions-russia-assets-freezes_en.pdf, question 5.

The Commission has also given its view on the control criteria. In the Commission notice of 1.9.2017¹⁰, the Commission has stated the following:

When assessing whether a legal person or entity is controlled by another person or entity, alone or pursuant to an agreement with another shareholder or other third party, it is necessary to carry out a factual assessment of all the organisational, structural and economic links between the two undertakings/entities.

The determining factor is whether the listed entity is able to and effectively asserts a decisive influence over the conduct of the other entity in question. Whilst a significant shareholding is one factor that may suggest control, there is no minimum threshold. Even a minority shareholding may be sufficient if it is allied to rights greater than those normally granted to minority shareholders and if ‘consistent legal or economic indicia’ show that the listed entity is in fact influencing the other entity.

The indicia of decisive influence include:

- a. the power to appoint or remove a majority of the members of the administrative, management or supervisory body of such legal person or entity;
- b. using all or part of the assets of a legal person or entity;
- c. sharing jointly and severally the financial liabilities of a legal person or entity, or guaranteeing them;
- d. having influence as regards corporate strategy, operational policy, business plans, investment, capacity, provision of finance, human resources and legal matters;
- e. putting in place or maintaining mechanisms to monitor the commercial conduct of the legal person or entity;
- f. other indicia such as sharing a business address or using the same name which could cause third parties to have the impression that the two entities are in fact part of the same undertaking.

2. What is the “ultimate beneficial owner” and why does it matter?

The Anti-Money Laundering legislation uses the term “ultimate beneficial owner” (UBO). In the process of determining the person who has control over the business partner, knowing the ultimate beneficial owner can prove useful.

An ultimate beneficial owner is any natural person who ultimately owns or controls a corporate entity or other legal entity and/or the natural person(s) on whose behalf a transaction or activity is being conducted. As a general rule of thumb (and without prejudice to the specific circumstances of a case), the ultimate beneficial owner of a legal entity may be the natural person who:

- holds an equity interest of at least 25%; or
- wields at least 25% of the voting rights; or
- is the beneficiary of at least 25% of the equity.

Other legal rights may confer control over the EU operator’s business partner to a person or entity who is subject to EU restrictive measures. Such rights may include the possibility to appoint the members of the management or supervisory board, to exercise a dominant influence on legal and business decisions or to act as a major financier. EU operators might consider referring to Article 3(6) of

¹⁰ Commission frequently asked questions on EU restrictive measures in Syria, https://finance.ec.europa.eu/system/files/2020-01/170901-faqs-restrictive-measures-syria_en.pdf.

Directive (EU) 2015/849 (Anti-Money Laundering Directive) in order to find further details on identifying beneficial owners for legal persons and legal arrangements.