



*presents*

# Foreign Asset Control Compliance in Domestic and International Transactions

## Avoiding Penalties in the New Enforcement Environment

**A Live 90-Minute Teleconference/Webinar with Interactive Q&A**

**Today's panel features:**

Judith A. Lee, Partner, **Gibson Dunn & Crutcher**, Washington, D.C.

Edward L. Rubinoff, Partner, **Akin Gump Strauss Hauer & Feld**, Washington, D.C.

Erin L. Crockett, Director, Corporate Global Trade Compliance, **Dresser**, Addison, Texas

**Tuesday, October 6, 2009**

The conference begins at:

**1 pm Eastern**

**12 pm Central**

**11 am Mountain**

**10 am Pacific**

The audio portion of this conference will be accessible by telephone only. Please refer to the dial in instructions emailed to registrants to access the audio portion of the conference.

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The background features a globe centered on South America, with labels for countries like Argentina, Brazil, and Uruguay, and cities like Santiago, Buenos Aires, and Asunción. A stack of books is visible on the left, with titles such as 'REAIS' and 'PASSARPO' partially legible. The text is overlaid on this background.

**STRAFFORD PUBLICATIONS**

**FOREIGN ASSETS CONTROL**

**Judith A. Lee**

**GIBSON, DUNN & CRUTCHER LLP**

**October 6, 2009**

# Office of Foreign Assets Control

- Administers and enforces economic and trade sanctions
- Based on U.S. foreign policy and national security goals
- Against targeted countries, terrorists, narcotics traffickers, and proliferators of weapons of mass destruction.



# Overview of U.S. Economic Sanctions Law

- Comprehensive Embargoes: Cuba, Iran and Sudan
- Prohibited dealings with the following, wherever located:
  - Cuban nationals
  - Entities owned or controlled by, or representing the governments of, Cuba, Iran and Sudan
  - Individuals or entities on the “SDN” List published by OFAC
- More limited sanctions apply to dealings with Syria, Burma (Myanmar), and North Korea
- U.S. persons prohibited from “facilitating” dealings by foreign persons that U.S. persons cannot directly undertake.

# COMPREHENSIVE SANCTIONS

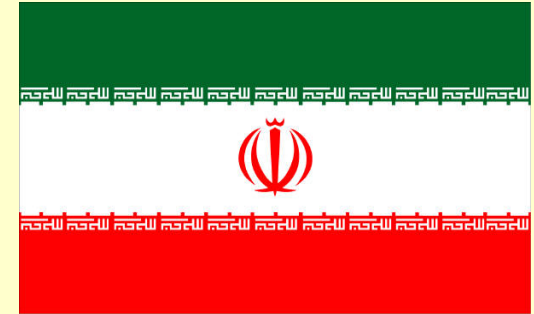
- **CUBA**

- **IRAN**

- **SUDAN**

- **Most transactions by U.S. persons in country or with governments prohibited**
- **Facilitation of activities of foreign persons prohibited**
- **No exports or transshipments of U.S. goods or from U.S.; no imports**
- **Re-exports of U.S. goods by foreign persons limited to EAR 99, 10% *de minimis* CCL or transformed CCL items; no ITAR components**

# IRAN



- Rejection vs. blocking of government assets (except SDNs)
- U.S. person may export with knowledge specifically for Iran if ascertain all four conditions are present:
  1. NLR (EAR 99)
  2. Incorporated into foreign good and <10% or substantially transformed
  3. No prohibited end-use under EAR
  4. Foreign items not intended or uniquely suited for use in petroleum or petrochemical industry
- Imports of carpets and foodstuffs may be authorized

# IRAN – Prohibited Dealing Abroad

- *Dealing*: The Regulations prohibit U.S. persons, wherever located, from engaging “in any transaction or dealing in or related to: (a) goods or services of Iranian origin or owned or controlled by the Government of Iran; or (b) goods, technology, or services for exportation, reexportation, sale or supply, directly or indirectly, to Iran or the Government of Iran.”
- The term “dealing” is defined to include “purchasing, selling, transporting, swapping, brokering, approving, financing, facilitating, or guaranteeing.”

# SUDAN



- Southern Sudan excluded from Sanctions:

Southern Sudan, Southern Kordofan/Nuba Mountains State, Blue Nile State, Abyei, Darfur

Marginalized areas in and around Khartoum

(official camps for internally displaced persons: Mayo, El Salaam, Wad El Bashir, and Soba)



# CUBA



- Most restrictive
- Includes Cuban nationals outside Cuba; must block funds
- TWEA – Foreign companies owned or controlled by U.S. person subject to restrictions
- Reexports by foreign persons not subject to policy of denial if < 20 percent U.S. content

# LIMITED SANCTIONS

- **BURMA  
(MYANMAR)**



- No financial services to Burma
- No imports of Burmese goods
- Exports and transactions unrelated to financial services allowed

# LIMITED SANCTIONS

- **SYRIA**



- **NORTH KOREA**



- No exports or re-exports of U.S. origin goods; even EAR 99
- General policy of denial (only applies to luxury goods and certain CCL items for North Korea)
- North Korean imports restricted
- Most services allowed
- No “facilitation” issues

# Other Sanctions

- Balkans
- Côte d'Ivoire (Ivory Coast)
- Congo
- Diamond Trade
- Iraq
- Lebanon
- Liberia
- Narcotics Trafficking
- WMD Nonproliferation
- Terrorism
- Zimbabwe

LARGELY ENFORCED THROUGH SDN LIST



# Risks – Foreign Subs

- **Facilitation Risks**
  - Approval/facilitation of acts prohibited to U.S. persons
  - U.S. persons working at foreign sub; recusal?
- **Blocking Statutes**
  - Cuba
  - Legislation pending to extend Iran sanctions to entities owned or controlled by U.S. persons
- **Re-exports**
  - Possible presumption of knowledge of specific destination
  - Involvement of U.S. logistics support

# Risks – Foreign Parents

## ■ **Re-export Risks**

- Unlawful re-exports
- Parent liability for procuring transshipment (innocent dupe)
- “General inventory” versus transshipment
- Knowing violations - U.S. subsidiary liability and/or conspiracy
- No EAR99 reexports to Syria or North Korea (unless 10%)

## ■ **Facilitation Risks**

- Advice on Cuba, Iran, Sudan, Burma transactions that are illegal for U.S. persons.

# Facilitation — Dealing Risk in Mergers and Acquisitions

- If there is revenue stream from an embargoed country, can change terms of deal
- Significant revenue from embargoed countries problematic
- If asset purchase, may need license prior to closing
- Due diligence and advance planning are critical



# General Inventory Guidance

## (July 7, 2002)

- U.S. exporter aware of re-exports to Iran from general inventory of distributor; concerned may happen again

- **OFAC DID NOT SAY LAWFUL OR UNLAWFUL:**

**MUST NOT EXPORT GOODS TO A THIRD PARTY IF HAVE REASON TO KNOW INTENDED SPECIFICALLY FOR IRAN.**

- **Numerous ways to have reason to know; facts indicating:**
  - Purchased specifically to fill Iranian order
  - Buyer deals exclusively or predominantly with Iran
  - Other factors: course of dealings, general knowledge, etc.

**CAUTION: NOT AN OFAC “EXCEPTION”**





# Information & Informational Materials Exemption

- Berman Amendment: IEEPA § 1702(b)(3); TWEA § 5(b)(4)
  - **Includes but not limited to publications, films, posters, phonograph records, photographs, microfilms, microfiche, tapes, compact disks, CD-ROMs, artworks, news wire feeds in any format or medium of transmission even if commercial products.**
- No CCL Items (e.g., no controlled technology or software)
- Traps for the unwary. OFAC interpretations may prohibit many related activities such as development of materials, marketing, distribution, and other activities without a license. Stricter restrictions may apply to actions with government entities and/or products that are not “written.”

# SDNs and Blocked Persons

- Person designated under various OFAC sanctions programs
- Over 3,000 persons/entities all over globe
- Transactions with an entity on the SDN List are prohibited
- Blocking (seizing) required; reports must be submitted to OFAC

# IEEPA Penalties Increased

- IEEPA Penalties (Iran, Sudan, Burma, Syria)
  - Max fine *increased* from \$50,000 to *\$250,000* per violation
  - Max confinement still *20 years*
  - Apply to violations where enforcement action was pending or commenced on or after October 16, 2007
- TWEA Penalties (Cuba and North Korea)
  - Max fine *\$1 million* for entities; \$100,000 for individuals
  - Max confinement *10 years*



# Concerns for Entities that Issue Securities in the United States

- SEC now demands enhanced disclosures on activities in sanctioned countries on the ground that such information could be qualitatively material
- SEC's Office of Global Security Risk works with OFAC regarding business in sanctioned countries

# Other Jurisdictions Have Prohibited Party Lists

- For example:
  - Bank of England list
  - United Nations list
  - Monetary Authority of Singapore
  - Most financial institutions have automatic screening against these lists

# Blocking Statutes



- Potential conflict of laws
  - European Union and Canada prohibit certain compliance with U.S. embargo on Cuba
  - Mexico prohibits compliance with any U.S. embargo
  - EU and Canadian laws require local subsidiaries to report instances where U.S. parent directs compliance with U.S. embargo against Cuba
  - Where conflict, can be difficult to resolve

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AKIN GUMP  
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## **Assuring Foreign Asset Control Compliance in Domestic and International Transactions: Avoiding Penalties in the New Enforcement Environment**

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### **OFAC Enforcement Environment**

**Edward L. Rubinoff**  
**Akin Gump Strauss Hauer & Feld**  
**October 6, 2009**



## Roadmap

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- Interim Enforcement Guidelines
- Voluntary Self-Disclosures
- Civil Penalty Process
- Audits and Investigations
- Recent Enforcement Actions: What can be learned?

## Interim Enforcement Guidelines

- Effective September 8, 2008 (73 Fed. Reg. 51933)
  - ◆ Supersede the old enforcement guidelines
  - ◆ Adopts uniform approach instead of industry-specific standards
- Driven by stiff increases in maximum penalties mandated by the IEEPA Enhancement Act of 2007
  - ◆ Civil penalties – up to \$250,000 per violation or twice the value of the transaction at issue
  - ◆ Criminal penalties – up to \$1 million per violation and/or 20 years imprisonment
- Interim Policy
  - ◆ OFAC will follow old enforcement guidelines where:
    - A Prepenalty Notice was issued prior to October 16, 2007 (date that the IEEPA Enhancement Act was signed into law)
    - OFAC staff recommended a proposed settlement amount under the old guidelines and that amount was memorialized in writing between the parties
    - Certain statute of limitations waivers are involved
  - ◆ All other cases are potentially subject to the new enforcement guidelines and statutory penalty amounts regardless of when violations occurred or VSDs were filed

## Interim Enforcement Guidelines

- Types of responses to apparent violations:
  - ◆ No action
  - ◆ Request for additional information
  - ◆ Cautionary letter (new option)
  - ◆ Finding of violation without civil penalty (new option)
  - ◆ Civil monetary penalties
  - ◆ Criminal referral
  - ◆ Other administrative actions (e.g., license denial, suspension, etc.)
  
- Eleven General Factors considered in determining appropriate enforcement response, including:
  - ◆ Willful/reckless violation
  - ◆ Awareness of conduct at issue
  - ◆ Harm to sanctions program objectives
  - ◆ Individual characteristics of the violator
  - ◆ Compliance program
  - ◆ Remedial response
  - ◆ Cooperation with OFAC

## Voluntary Self-Disclosures

- Only if self-initiated before discovery by OFAC or other U.S. Government agency
- No credit will be given for a VSD if it is:
  - ◆ Submitted after a blocking or rejection report has been received
  - ◆ False or misleading information
  - ◆ Materially incomplete
  - ◆ Directed or suggested by a regulator
- Must include (or be followed within a reasonable period of time by) a report providing sufficient detail to afford a complete understanding of an apparent violation's circumstances
- However, even if not given credit as a VSD, it will be valued in terms of cooperation with OFAC
- Earns 50% reduction in applicable base penalty amount

## Civil Penalty Process

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- Prior to imposing penalty, OFAC will issue a Prepenalty Notice
  - ◆ Describes alleged violation, relevant General Factors, proposed penalty and maximum penalty
  - ◆ Subject person will have opportunity to respond prior to issuance of Final Notice
- Settlements still available, but negotiated in accordance with new guidelines
- Penalties based on:
  - ◆ Egregious or non-egregious nature of violation
  - ◆ Whether violation was voluntarily self-disclosed

## Civil Penalty Process

The new enforcement guidelines provide the following matrix for determining base civil penalty amounts:

		<u>Egregious Case</u>	
		No	Yes
<u>Voluntary Self-Disclosure</u>	Yes	(1) One-Half of Transaction Value (capped at \$125,000 per violation)	(3) One-Half of Statutory Maximum
	No	(2) Applicable Schedule Amount (seven categories from \$1,000 to \$250,000 based on transaction value)	(4) Statutory Maximum

## Civil Penalty Process

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- Base penalty amount may be adjusted based on evaluation of General Factors
- Substantial cooperation with OFAC results in 25-40% reduction in base penalty
- First violation typically results in reduction of up to 25% of base penalty
- Prescribed penalty amounts for failure to furnish information or keep records

## Audits and Investigations

- Historically, OFAC has not conducted a great deal of audits or investigations of companies or individuals.
- This is changing. OFAC has been spending more resources and becoming more active in this area.
- New OFAC enforcement officials come from a prosecutorial background
- In the past, OFAC sent letters requesting information from various parties for investigative purposes. Now OFAC has begun sending administrative subpoenas.
- These efforts are targeting potential violations that involve sensitive regions and transfers (e.g., transfers of export-controlled items to Iran)



## Recent Enforcement Actions: DHL

DPWN Holding (USA) and DHL Express (USA) (collectively “DHL”) allegedly made numerous shipments to Iran and Sudan in violation of the OFAC regulations, made certain unlicensed exports to Syria in violation of the EAR, and failed to maintain adequate records with respect to these shipments.

- ◆ Settled these alleged violations with BIS and OFAC for \$9,444,744
- ◆ Due, in part, to a waiver of the statute of limitations, penalties were brought under the old IEEPA provisions
- ◆ The majority of the penalties came from recordkeeping violations, but involved over 30,000 violations totaling a preliminary prepenalty of over \$320 million
- ◆ No voluntary disclosure was filed with BIS or OFAC – but substantial mitigation applied notwithstanding (97%), apparently because shipments involved mostly informational materials
- ◆ Required to conduct audit and report to OFAC and BIS

## Recent Enforcement Actions: DHL

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### Observations

- ◆ Strong message sent regarding the importance of maintaining compliance records
- ◆ Focus on freight forwarders – critical cogs in export chain who share compliance responsibilities with exporters
- ◆ Suggests increased cooperation between enforcement agencies with overlapping jurisdiction

## Recent Enforcement Actions: ASI

Aviation Services International, B.V., a Dutch aviation services company, and its director and sales manager plead guilty to criminal charges of conspiracy to illegally export aircraft components to Iran through the Netherlands, Cyprus, and the UAE

- ◆ Involved willful violations of IEEPA and the Iranian Transaction Regulations resulting in exports to Iran of U.S.-origin components that could be used in unmanned aerial vehicles
- ◆ Penalties brought under IEEPA Enhancement framework:
  - Company - \$100,000 fine and five years of corporate probation
  - Individuals (Dutch citizens) – Potential 5 years in prison and a maximum fine of \$250,000 or twice the pecuniary loss/gain
- ◆ Investigation conducted by BIS, ICE and the FBI

## Recent Enforcement Actions: Oxbow

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Oxbow Carbon and Minerals LLC, a U.S. company, engaged in transactions and facilitated other transactions by non-U.S. persons involving the use of vessels owned/managed by the Islamic Republic of Iran Shipping Lines in Tehran.

- ◆ Remitted \$276,250 to settle this alleged violations of the Iranian Transaction Regulations
- ◆ Settled under old enforcement guidelines
- ◆ Did not file a VSD but did cooperate with OFAC during review
- ◆ Revised its compliance program

## Recent Enforcement Actions: ANZ

Australia and New Zealand Bank Group (“ANZ”) allegedly violated the Sudanese Sanctions Regulations and Cuban Assets Control Regulations in its international trade finance and foreign currency exchange activities. The bank manipulated SWIFT messages to conceal the identities of entities subject to U.S. sanctions and thereby impeded the ability of U.S. banks to detect these violations. The transaction values totaled over \$100 million.

- ◆ Remitted \$5,575,000 to settle the allegations
- ◆ Apparently resolved under new Interim Enforcement Guidelines
- ◆ Engaged in substantial cooperation and undertook a “prompt and thorough” remedial response, but did not voluntarily disclose
- ◆ Demonstrated history of OFAC compliance
- ◆ Agreed to examine and revise policies to ensure compliance and report findings to OFAC

## Recent Enforcement Actions: Stena Bulk

Stena Bulk LLC, a subsidiary of one of the world's leading tanker shipping companies, allegedly violated the Sudanese Sanctions Regulations by facilitating transactions with Sudan on behalf of foreign entities. It allegedly transported oil to and exported oil from Sudan without an OFAC license.

- ◆ Remitted \$426,486 to settle the allegations
- ◆ Involved a transaction targeted by the sanctions program (i.e., Sudanese petrochemical industry)
- ◆ Appears to have been settled under the new enforcement guidelines

## Recent Enforcement Actions: GSR

Gold & Silver Reserve, Inc. (“GSR”) engaged in the exportation of financial services that allegedly violated the Iranian Transaction Regulations and the Cuban Assets Control Regulations. GSR activated 56,739 “e-currency” accounts through its website to persons located in Iran and dealt in property, in the form of 69 “e-currency” accounts, in which Cuban nationals had an interest.

- ◆ Assessed a \$2,950,000 civil penalty
- ◆ Penalties issued under old IEEPA framework
- ◆ Also agreed to a criminal forfeiture of \$1,750,00 and a criminal penalty of \$300,000
- ◆ OFAC released the Penalty Notice = Unprecedented

## Recent Enforcement Actions: What can be learned?

- Dedication of additional resources to enforcement
- More aggressive enforcement, particularly for violations involving scrutinized regions and transactions (as opposed to focusing on Cuba travel)
- More Iran cases targeting industries that facilitate third country trade with Iran (banks, shipping, insurance)
- Only a few cases settled under new enforcement guidelines - a backlog of cases awaits
- Increasingly higher penalty amounts as cases are resolved
- Increased cooperation among OFAC, BIS, and DOJ in investigations and enforcement cases
- Incentives to submit voluntary disclosures and cooperate with OFAC review
- Importance of implementing and following an OFAC compliance program





# **BEST PRACTICES** **for Companies**

Foreign Assets Controls Compliance

October 6, 2009



Erin L. Crockett

Dresser Inc.

Director Global Trade Compliance



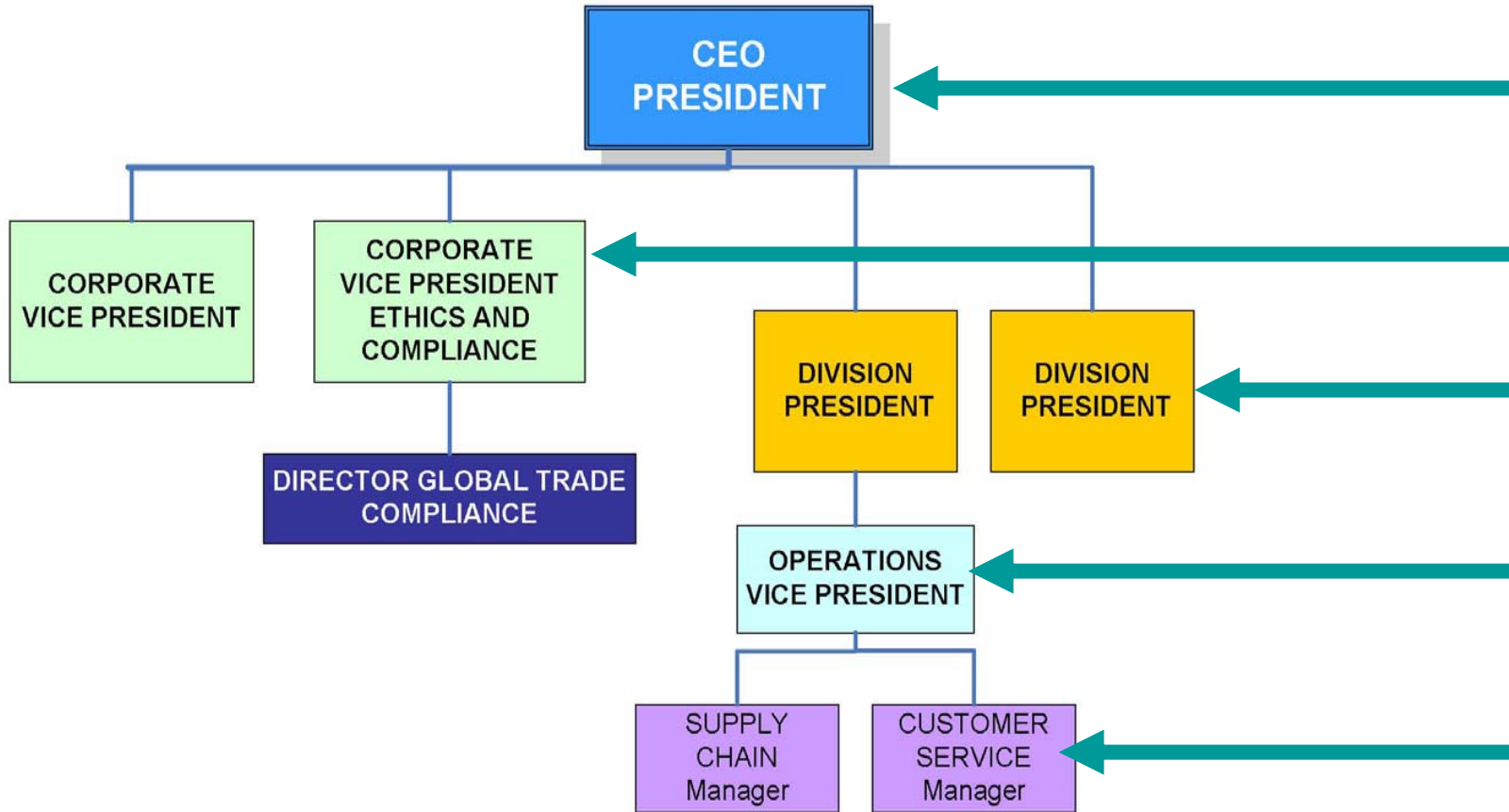
# Trade Compliance Program

- Tone at the Top!



**Board's Audit Committee,  
Top Management, etc.**

# Tone **STARTS** at the Top . . . but **Must work its way** **Down!**





# Trade Compliance Program

- Tone at the Top!
- Structure / Reporting lines of the Global Trade Compliance group
- Risk assessments / Audits / Reviews – **Monitoring & Reporting**
- Investigations
- CIP – “Continuous” Compliance Improvement Program(s)
  - **Roots cause analysis**
  - **Corrective action**
  - **Monitoring**

# Trade Compliance Program cont'd

- Trade policy and procedures
  - Robust program
    - Periodic updates and revisions
  - Special procedures for transactions subject to the OFAC regulations
    - Facilitation
    - Guidance – “Prohibited under Regulations or Policy”
- Compliance manual and desktop instructions



# Restricted Party Screening



- Belarus, Burma and others . . .
  - OFAC Guidance
    - U.S. Treasury Department’s Office of Foreign Assets Control (“OFAC”) – List of Specially Designated Nationals (the “SDN” list)
    - Published Guidance – designation applies to **any** entities in which Belneftekhim owns, directly or indirectly, **50% or greater interest**
    - But not just Belneftekhim – any “blocked” party
  - BIS Guidance
    - **Revised rule** explicitly applies not only to exports or reexports to Burmese entities on the SDN list, but also to persons or entities in which a blocked Burmese SDN owns a 50 percent or greater interest even if that person or entity is not specifically named on the SDN list
    - BIS adopted this 50 percent rule to *match* OFAC’s similar policy
    - Greatest impact to foreign companies, since U.S. companies and other U.S. persons are already generally prohibited from exporting to SDNs

**Screening is getting more difficult!**

## Trade Compliance Program cont'd

# Education, Education, Education!



- More than one time!
- Keep updated
- Reduce complex Sanction Regulations down to simplistic concepts
- If global – consider translations or interpreters

# Company Policy versus Law . . .

- Some companies have withdrawn from conducting business with one or more of the U.S. economic sanctioned countries



**HALLIBURTON**



imagination at work

**DRESSER-RAND**





# But Some Companies Can and Do Continue

- Strong Internal Controls
- Thorough Understanding of the regulations
- Periodic Internal Reviews
- Solid Inventory controls
  - **Bona Fide General Inventory**
  - **Special Orders?**
  - **De Minimis**
    - Repair
    - Replacement
- Do not forget General Prohibition 10!

# Hints Along the Way . . .



- Understanding U.S. Persons . . .  
Incorporation Structure
  - e.g., United Arab Emirates company registered as “Inc.” = U.S. branch versus subsidiary
- Sales by Country Reports
  - Look also at sales into a Region or Country that is destined for transshipment or transfer
- Transshipment Points of Concern
  - Jebel Ali Free Zone
  - Singapore
  - Malaysia





# Diversion Risks Are Real!

- Your Dubai office GM calls to advise that he just returned from a visit with the Dubai Customs Authorities regarding a shipment Dubai Customs is holding before it exports to Iran



## How did you end up in this situation

If your company policy is no new business with Iran?

OFAC and BIS regulations require an export license to Iran?

If your records indicate you exported the goods to Canada?

# What Happened . . .



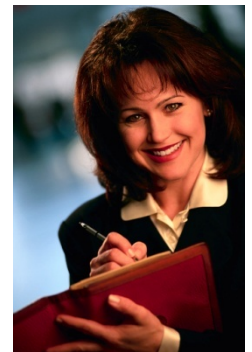
# Due Diligence on Channel Partners

- Questionnaires
- Checklist
- Background Checks
- Annual Reviews
- Agreement Clauses
  - **Compliance with U.S. laws and local laws**
  - **Right to Audit**
- Education
  - **Not Legal advice**
  - **Not Compliance group**



# M&A – Always a Concern

- In today's global environment – strong due diligence important!
  - Sufficient questions
  - Ask point blank regarding sales to U.S. sanctioned countries
  - Where are offices located
    - Sanctioned countries locations?
    - UAE location?
  - Sales by Countries / Regions, etc.
  - How to handled existing contracts based on your company policy?
  - Is a Disclosure necessary?



# Let's Not Forget Joint Ventures

- Who has majority ownership?
- Is there an agreement regarding export control compliance?
- What is the structure of the JV board?
- Do any board members need to sign a Recusal to ensure no facilitation actions?



**Thank you!**



**Questions?**