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## OFFICE OF FOREIGN ASSETS CONTROL: THE LITTLE AGENCY WITH A BIG BITE

*Administered by the U.S. Treasury, OFAC sanction programs are unique in that they can involve both exports of goods and services, and financial transactions. The authors review the mitigating factors in recent cases involving major settlements with financial institutions and from them distill protective features for compliance programs designed to minimize OFAC risks.*

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With over a billion dollars in fines to its credit in the past few years, the Treasury Department's Office of Foreign Assets Control (OFAC) is no longer an obscure office known only to corporate compliance officers. But knowing that OFAC exists is only the first step in coming to grips with how to include OFAC as part of the entire constellation of corporate compliance programs. Given its unique applicability to both exporting goods and services, and to financial transactions generally, corporate leaders in the banking and financial services industries might benefit from an improved understanding of OFAC's role. After briefly introducing where OFAC fits in the compliance universe, this article will discuss several OFAC enforcement matters and offer general guidance for executing a risk-based corporate compliance program.

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### OFAC'S PLACE IN THE COMPLIANCE UNIVERSE

OFAC's programs cover U.S. sanctions objectives by country, or by policy objective, such as preventing proliferation of weapons of mass destruction. Other compliance programs cover goods, generally, such as those under the Export Administration Regulations and the International Traffic in Arms Regulations, administered by the Departments of Commerce and State, respectively. More familiar, perhaps, to professionals in banking and financial services are transactional compliance programs, like anti-money laundering (AML) regulations under the Bank Secrecy Act (BSA) and Foreign Corrupt Practices Act (FCPA). OFAC's programs are unique, since they can involve both export restrictions on goods and services, as well as controls on financial transactions. Additionally, one

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might be in compliance with other programs, but still be in violation of an OFAC regulation. As a result, OFAC compliance can present a trap for the unwary. This is especially true in cases where U.S.-based multinational corporations may be able to do business in sanctioned countries through subsidiary business units.

Since Iran is a major focus in U.S. foreign policy, a few Iranian examples will help illustrate potential traps. Subsidiaries of a U.S. company typically may be able to undertake certain types of business in Iran, provided that U.S. persons do not participate in the subordinate's transaction. So, if a foreign subsidiary sold construction materials to an Iranian company, or to a company in a third-party country for use in Iran, such activity is typically not prohibited by the OFAC-administered Iranian Transactions Regulations (ITR). However, if the very same sale of materials included approval, direction, oversight, or other facilitation by corporate personnel who are U.S. persons, or who are present in the United States, then the parent company would be in violation of the ITR. Such a situation might arise when a corporate policy requires subordinates to gain higher approval for bids or sales over a particular dollar amount. Another Iran-focused example applies to exports of goods or services. Typically, a company may provide banking services or write insurance policies in foreign countries as a legitimate part of normal business. However, if a U.S. company provides services with knowledge that the ultimate beneficiary is Iranian, or the Government of Iran, then that conduct could violate the ITR. The Iranian case can be particularly challenging, since a 2010 change to the ITR basically gave OFAC the authority to define the term "Government of Iran" to include any party that benefits an Iranian interest.<sup>1</sup> Entities in Japan, Germany, and Italy, among others, were subsequently found to be the "Government of Iran" by OFAC.<sup>2</sup>

The U.S. sanctions on Cuba, however, present additional difficulties because, unlike the other U.S. sanctions programs, the Cuba sanctions apply directly to foreign subsidiaries of U.S. companies. Canada is an example where national law prohibits Canadian

companies and individuals from complying with the U.S.–Cuba embargo. A U.S. subsidiary in Canada simultaneously obeys U.S. law and violates Canadian law when it refuses to conduct a transaction in Canada that touches on Cuba. Unfortunately, there is no easy remedy for this conflict of laws caused by the global scope of U.S. sanctions against Cuba.

## RECENT HISTORY OF AGGRESSIVE ENFORCEMENT BY OFAC

The United States has shown increasing vigor in using sanctions programs to achieve foreign-policy objectives. The wave of unrest in the Middle East provides the example of Libya, where the President issued an executive order imposing sanctions shortly after Libyan Government efforts to quell protests turned violent.<sup>3</sup> The President also recently expanded sanctions against Syria.<sup>4</sup> The sanctions activity around events in the Middle East also shows the need for compliance programs to be agile and responsive, as business engagements that are entirely acceptable may become proscribed on very short notice. Recently announced indictments also demonstrate that OFAC enforcement remains aggressive. The Department of Justice (DOJ) announced an indictment in February 2011 against four family members charged in a scheme to export military aircraft jet engines to Iran.<sup>5</sup> And in late April 2011, DOJ announced an indictment of a New York businessman and his associates on charges of exporting computer equipment to Iran via a third-party country.<sup>6</sup>

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<sup>3</sup> Executive Order 13566, 76 Fed. Reg. 11,315 (Mar. 2, 2011).

<sup>4</sup> The White House, Office of the Press Secretary, Executive Order, Blocking Property of Certain Persons with Respect to Human Rights Abuses in Syria, Apr. 29, 2011, *available at*: [http://www.treasury.gov/resource-center/sanctions/Documents/110429\\_syria.pdf](http://www.treasury.gov/resource-center/sanctions/Documents/110429_syria.pdf) (accessed May 2, 2011).

<sup>5</sup> Press Release, DOJ, Four Family Members Charged in Conspiracy to Export F-5 Fighter Jet Engines to Iran (Mar. 23, 2011), *available at* <http://www.justice.gov/usao/fls/PressReleases/110323-02.html>.

<sup>6</sup> Press Release, DOJ, Three Individuals and Two Companies Indicted for Conspiring to Export Millions of Dollars' Worth of

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<sup>1</sup> 75 Fed. Reg. 34,630 (June 18, 2010).

<sup>2</sup> 75 Fed. Reg. 48,562 (Aug. 11, 2010).

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Though the final results from the recent indictments are not yet known, it is well established that OFAC penalties and settlements have increased in the past few years. Starting with the massive settlements with Credit Suisse and Lloyds Bank at the very end of 2009, for example, OFAC settlements and penalties totaled nearly a billion dollars over the 13-month period that ended in December 2010. A review of some of the major OFAC enforcement actions, starting from the Credit Suisse and Lloyds settlements in December 2009 through the end of 2010, offers insight into the factors that compliance officers should consider in the design and execution of their programs.

### ***Credit Suisse Securities (USA) LLC***

In December 2009, Credit Suisse Securities (USA) LLC agreed to pay a \$536 million fine to settle alleged violations of numerous sanctions programs over a 20-year period.<sup>7</sup> Credit Suisse came forward to OFAC in multiple disclosures over the course of 2006, identifying that an internal investigation had revealed possible improper conduct relating to U.S. securities transactions executed on behalf of an entity subject to U.S. sanctions. Additionally, Credit Suisse informed OFAC of a separate internal investigation, related to the bank's activities as a U.S. dollar (USD) correspondent for payments involving sanctions targets, including Iran, Sudan, Burma, Cuba, North Korea, and persons whose property and interests in property were blocked pursuant to OFAC regulations. The multiple investigations revealed that Credit Suisse had systematically avoided U.S. bank filters by stripping references to sanctioned entities, especially Iranian, when processing USD transactions. These practices included omitting or removing information on sanctioned locations, entities, or individuals, to avoid disclosure of their true identities. One example of Credit Suisse's conduct was the insertion of Credit Suisse's name, or generic terms like "order of a customer," in place of the sanctioned parties in payment messages. Without admitting guilt, Credit Suisse agreed to pay a \$536 million fine to settle alleged violations of the International Emergency Economic Powers Act ("IEEPA"), the Trading with the Enemy Act, various executive orders, and associated sanctions regulations. Although the OFAC settlement did not disclose the base penalty amount, OFAC considered the

matter "egregious," based on Credit Suisse's systematic conduct over a 20-year period. But, in the settlement, OFAC also noted that Credit Suisse voluntarily disclosed the conduct, fully cooperated with OFAC, took appropriate remedial measures, and had not had a penalty notice or finding of violation within the previous five years. Even with a massive fine, OFAC said that the "resulting penalty would have assuredly been higher" if Credit Suisse had not cooperated with the investigations.

### ***Lloyds TSB Bank, PLC***

Less than a week after the Credit Suisse announcement, OFAC announced a \$217 million settlement with Lloyds TSB Bank, plc.<sup>8</sup> The close proximity in time is matched by the substantially similar conduct at issue in both the Credit Suisse and Lloyds settlements. Lloyds' employees engaged in a systematic pattern of removing identifying information for sanctioned entities when processing USD transactions. Over a three-year period, Lloyds routed over 4,000 transactions, worth more than \$35 million, through third-party banks located in the United States. The transactions were in apparent violation of IEEPA, and the OFAC regulations related to Iran, Sudan, and Libya. Lloyds did not voluntarily disclose the conduct. Terms of the settlement included Lloyds' agreement to perform annual audits, for two years, of the bank's policies and procedures, supervised by the United Kingdom's Financial Services Agency. Lloyds also agreed to conduct a statistically significant sampling of USD payments to determine whether payments that violate OFAC regulations were being processed through, or on behalf of, U.S. entities. OFAC deemed that the \$217 million fine had been satisfied by Lloyds' prior \$350 million payment to the DOJ and the New York County District Attorney's Office, arising out of the same pattern of conduct. The actual Lloyds settlement document is worth reading, because it describes some of the internal discussions that took place at Lloyds regarding the risks associated with non-compliance.<sup>9</sup> The Lloyds case illustrates the fundamental tension that banking and finance decision makers face when business opportunity and sanctions compliance pull in opposite directions.

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Computer-Related Equipment to Iran (Apr. 21, 2011), *available at* <http://www.justice.gov/opa/pr/2011/April/11-nsd-503.html>.

<sup>7</sup> OFAC, Enforcement Information for December 16, 2009 (Dec. 16, 2009), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/pages/20091216.aspx>.

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<sup>8</sup> OFAC, Enforcement Information for December 22, 2009 (Dec. 22, 2009), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/pages/20091222.aspx>.

<sup>9</sup> The settlement document is available at the link provided in note 8, *supra*.

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### **Agar Corporation, Inc. (“ACI”)**

OFAC alleged that ACI exported metering equipment valued at \$444,887 to its affiliate in Venezuela from April to June 2005, with knowledge that the equipment would be incorporated into items sent to Sudan, in violation of the Sudanese Sanctions Regulations.<sup>10</sup> The violation was not voluntarily disclosed. ACI settled by payment to OFAC of \$860,000, with a computed base penalty of \$1,967,098. While OFAC considered the alleged violations to be egregious, based on a perceived intent to evade sanctions, the settlement reflected: (1) ACI’s cooperation with the Bureau of Immigration and Customs Enforcement and OFAC; and (2) a plea agreement with the DOJ, pursuant to which ACI pleaded guilty to one count of violating IEEPA. ACI further agreed to pay a total criminal penalty of \$1,140,000, accept four years’ probation, which included an agreement to implement a comprehensive U.S. sanctions compliance program, and to enter into a tolling agreement with OFAC.

### **United Nations Federal Credit Union (“UNFCU”)**

OFAC alleged that UNFCU violated the Cuban Assets Control Regulations (“CACR”) by engaging in unauthorized financial transactions and services on behalf of members/accountholders who were blocked Cuban nationals.<sup>11</sup> The violations were not voluntarily disclosed. UNFCU settled by payment of \$500,000, with a computed base penalty of \$5,237,100. Mitigation was enhanced by UNFCU’s: (1) cooperation with OFAC; (2) agreement to conduct a CACR compliance review and report the results to OFAC; (3) agreement to take remedial measures to augment its OFAC compliance program; (4) base penalty amount, which was attributable in significant portion to many substantially similar alleged violations; and (5) absence of prior OFAC violations.

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<sup>10</sup> Press Release, DOJ, Houston Company Pleads Guilty to Illegally Facilitating Exports to Sudan (June 22, 2010), *available at* <http://www.justice.gov/usao/txs/releases/June%202010/062210%20Agar%20Corporation%20Inc.htm>; OFAC, Enforcement Information for July 15, 2010 (July 15, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/07152010.pdf>.

<sup>11</sup> OFAC, Enforcement Information for July 15, 2010 (July 15, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/07152010.pdf>.

### **Innospec, Inc.**

Innospec settled allegations of CACR violations arising out of business transactions in Cuba by an acquired subsidiary, in which the government of Cuba and/or Cuban nationals had an interest.<sup>12</sup> Specifically, the subsidiary ran afoul of the CACR by maintaining local sales offices in Cuba, by incurring general operating expenses, and by holding accounts in Cuban financial institutions. The violations were voluntarily disclosed. The matter was settled by payment of \$2,200,000, with a computed base penalty of \$4,447,878. Mitigating factors included: (1) Innospec’s cooperation with OFAC’s investigation, which included entry into a tolling agreement, as well as the firm’s cooperation with investigations of other U.S. and United Kingdom (U.K.) entities; (2) remedial measures, including selling the affected subsidiary to a non-U.S. third party and instituting compliance program enhancements; and (3) the fact that the OFAC settlement was part of a \$40,200,000 comprehensive criminal and civil settlement between Innospec and OFAC, DOJ, the Securities and Exchange Commission, and the U.K.’s Serious Fraud Office involving, among other things, guilty pleas to wire fraud and FCPA violations for certain dealings with Iraqi and Indonesian officials.

### **Barclays Bank PLC**

Much as was the case in the Credit Suisse and Lloyds Bank matters discussed earlier, Barclays allegedly circumvented U.S. bank filters, installed to detect transactions with U.S. sanctions targets, in at least 1,285 electronic funds transfers.<sup>13</sup> The transfers, conducted

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<sup>12</sup> Press Release, DOJ, Innospec Inc. Pleads Guilty to FCPA Charges and Defrauding the United Nations; Admits to Violating the U.S. Embargo Against Cuba (Mar. 18, 2010), *available at* <http://www.justice.gov/opa/pr/2010/March/10-crm-278.html>; OFAC, Enforcement Information for March 19, 2010 (Mar. 19, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/03192010.pdf>.

<sup>13</sup> Press Release, DOJ, Barclays Bank PLC Agrees to Forfeit \$298 Million in Connection with Violations of the International Emergency Economic Powers Act and the Trading With the Enemy Act (Aug. 18, 2010), *available at* <http://www.justice.gov/opa/pr/2010/August/10-crm-933.html>; OFAC, Barclays Bank PLC Settles Allegations of Violations of Multiple Sanctions Programs (Aug. 18, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/barclays08182010.pdf>.

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between August 2002 and September 2006 in violation of Sudanese, Iranian, Cuban, and Burmese sanctions, had an approximate aggregate value of \$112,695,000. The violations were voluntarily disclosed. The matter was settled by payment of \$176 million, with a calculated base penalty of \$218,971,000. The obligation was deemed satisfied by Barclays' payment of \$298 million to the DOJ and the New York District Attorney's Office in a related criminal proceeding. Aggravating circumstances included the alleged recklessness of the violations, awareness of the conduct by relevant managers, and Barclays' sophistication. Mitigating factors included: (1) Barclays' substantial cooperation, entry into tolling agreements, and other remedial efforts; (2) the lack of any OFAC penalty notices in the five years preceding the improper transactions; and (3) the fact that a number of the Sudanese transactions involved the export of agricultural products.

***Balli Group PLC, and Balli Aviation Ltd. (collectively, "BALLI")***

OFAC alleged that Balli exported three commercial airliners from the United States to Mahan Airlines in Iran, and further attempted to export three additional commercial airliners to Mahan, in violation of the ITR and the EAR.<sup>14</sup> The violations were not voluntarily disclosed. Balli entered a settlement with OFAC and the Commerce Department's Bureau of Industry and Security (BIS). Provisions included: (1) payment of a \$15-million civil penalty (\$2 million of which would be suspended if there were no further export control violations); (2) retention of a third-party consultant to conduct annual external audits of corporate compliance with U.S. export control laws and sanctions regulations for five years, including submission of the audit results to BIS and OFAC; and (3) BIS's suspension of Balli's export privileges for five years (although BIS agreed to suspend the denial order as long as the penalty was timely paid and if the company remained compliant with the settlement agreement and the EAR). In a related criminal case, Balli Aviation pleaded guilty and paid a \$2 million fine for illegally exporting commercial aircraft from the U.S. to Iran.

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<sup>14</sup> Press Release, DOJ, U.K. Firm Pleads Guilty to Illegally Exporting Boeing 747 Aircraft to Iran (Feb. 5, 2010), *available at* <http://www.justice.gov/opa/pr/2010/February/10-nsd-131.html>; OFAC, Enforcement Information for February 5, 2010 (Feb. 5, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/02052010.pdf>.

***Maersk Line, Limited and its Wholly Owned U.S. Subsidiaries (collectively, "MLL")***

OFAC alleged that MLL violated the Sudanese Sanctions Regulations and the ITR by providing unlicensed shipping services for 4,714 shipments of cargo originating in, or bound for, Sudan and Iran from January 2003 to October 2007.<sup>15</sup> The violations were not voluntarily disclosed. The matter was settled for \$3,088,400, with a computed base penalty of \$61,768,000. Aggravating factors included MLL's sophistication and the harm to sanctions program objectives by conferring economic benefits on Sudan and Iran. Mitigating factors included: (1) no violations of OFAC sanctions in the preceding five years; (2) full cooperation with OFAC's investigation of the alleged violations, including entry into two tolling agreements; (3) substantial remediation measures; and (4) the fact that the base penalty amount considered the gross freight charges for shipping the cargo from origin to destination, although the apparent violations involved only a portion of those voyages.

**OFAC AWARENESS IN A COMPLIANCE PROGRAM**

The scope and magnitude of OFAC enforcement penalties are increasing in response to sanctions violations. These developments parallel the trend by U.S. administrations to increasingly use sanctions programs as behavior-shaping tools in foreign policy. Even in a global-scale business, a fine denominated in the hundreds of millions of dollars is serious money, and should generate serious interest in effective compliance. OFAC enforcements increasingly include criminal dimensions, raising the stakes even further. Worldwide corporate reach raises the risk, given the network of financial flows in the global economy. In addition to higher risk, global scale may also result in more severe penalties, since sophisticated participants in the financial system are held to higher standards.

Businesses must respond to the changing enforcement landscape by establishing effective internal controls. Deep scrutiny of every transaction would be wasteful, but a risk-based approach can identify potential concerns, with minimal impact on operations. Penalty magnitude is strongly influenced by aggravation and mitigation factors, and by whether disclosure of the behavior is voluntary. As a result, prudent internal

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<sup>15</sup> OFAC, Enforcement Information for July 28, 2010 (July 28, 2010), *available at* <http://www.treasury.gov/resource-center/sanctions/OFAC-Enforcement/Documents/07292010.pdf>.

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controls and swift reporting when potential violations are found are critical factors in reducing risk. A general list of protective considerations is:

- a) risk-based assessment of vulnerabilities associated with transactions, based on their magnitude, location, and the history of prior dealing;
- b) training for personnel involved with cross-border transactions, to sensitize them to the potential risks, and to provide guidance on what procedures should be followed in the event that possible inappropriate activity is discovered;
- c) escalation provisions that allow senior compliance officials to evaluate unusual situations detected by employees; this allows problems to be avoided, or minimized, and rapidly reported if they do occur;
- d) routine monitoring of compliance procedures to verify operation within established parameters;
- e) preplanned responses established by corporate leadership to ensure that possible violations are correctly reported. Because promptness is a factor, leaders should have had discussions in advance about what will be done, and who will do it, when apparent violations are to be reported. A time-consuming internal investigation to gain greater fidelity about whether a violation actually occurred may not be the most prudent approach.

Banking and financial services professionals are usually most familiar with the compliance programs supervised by the Department of the Treasury's Financial Crimes Enforcement Network (FinCEN). Those BSA/AML programs are frequently executed in concert with FCPA compliance. But the massive fines recently paid by Credit Suisse, Lloyds, and Barclays reveal that OFAC is much more "bite" than "bark." Though perhaps less well-known, Treasury's OFAC regulations should be a focus area in any comprehensive, risk-based compliance program. ■