



POLICY ALERT // MAY 9, 2019

OFAC Releases Detailed Compliance Expectations

The Treasury Department’s Office of Foreign Assets Control (OFAC) published its Framework for OFAC Compliance Commitments (“OFAC Compliance Guidance”) on May 2, 2019. The guidance is the most extensive, consolidated articulation of OFAC’s compliance expectations to date. Although it notably stops short of mandating a sanctions compliance program, the guidance provides a description of common compliance pitfalls seen in its enforcement actions to help companies in complying with sanctions. The guidance follows a recent spike in OFAC enforcement activity targeting a wide variety of compliance failures.

- ▶ OFAC calls for a risk-based approach to sanctions compliance, with a company’s size, products and services, and geographic locations informing risk.¹ The emphasis on the risk-based approach brings OFAC compliance expectations more closely in line with those expectations identified by anti-money laundering (AML) and other federal regulators.
- ▶ While OFAC recognizes that its regulations do not require a formal sanctions compliance program, it makes clear in the OFAC Compliance Guidance that lack of an effective compliance program is a root cause for sanctions violations and a factor in pursuing enforcement actions.
- ▶ OFAC underscores that it will exercise broad jurisdiction over U.S. and non-U.S. organizations and individuals. In one of the clearest statements of its jurisdiction, OFAC encourages organizations directly subject to U.S. jurisdiction, as well as foreign entities that conduct business in or with the United States, U.S. persons, or using U.S.-origin goods or services, to employ a risk-based approach to compliance with U.S. sanctions.²

The OFAC Compliance Guidance comes as sanctions are being used more aggressively across a range of programs, including by targeting central banks, companies with significant market shares in major industries, and sanctions evaders who use front and shell companies to hide their illicit activities.

Compliance officers will face an increasingly complex sanctions environment and must continue to understand and mitigate these risks.

[Overview of OFAC’s Framework for Compliance Commitments](#)

OFAC’s guidance establishes a “five-pillar” framework for compliance programs that is employed in other regulatory contexts such as for AML programs. In



doing so, the OFAC Compliance Guidance builds on compliance guidance from the Federal Financial Institutions Examination Council (FFIEC) *Bank Secrecy Act/Anti-Money Laundering Examinations Manual* and the Department of Justice *Evaluating Corporate Compliance Programs*.³ These pillars are:

- ▶ **Senior management should demonstrate a commitment to supporting an organization’s sanctions compliance program.** Like other regulatory agencies, OFAC expects senior management to review and approve its company’s program, maintain an autonomous and well-resourced compliance unit, and promote a culture of compliance within its organization.⁴ This means designating a specific OFAC compliance officer (who could also be serving in other compliance functions, such as the Bank Secrecy Act officer) and ensuring that compliance staff sufficiently understand OFAC regulations and can identify OFAC-related issues, risks, and prohibited activities.
- ▶ **Organizations should conduct routine risk assessments in order to identify potential sanctions risks. OFAC recognizes that there is no “one-size-fits all” risk assessment, but suggests that organizations conduct holistic reviews to identify areas where they may be exposed to sanctions-related risk.** Sanctions risk may be introduced into an organization by customers, counterparties, supply chains, products, services, and geographies.⁵ Sanctions risk assessments should also be standard practice when onboarding outside parties or preparing a merger or acquisition.⁶
- ▶ **Organizations should maintain documented internal controls to “identify, interdict, escalate, report (as appropriate), and keep records” of activity implicating OFAC regulations.** Previously, the FFIEC set forth expectations for financial institutions to screen customers and counterparties against OFAC designated persons.⁷ OFAC’s guidance makes clear that these expectations apply beyond the financial services industry and go beyond basic screening requirements. Exact requirements depend on the organization’s risk assessment. Internal controls must be monitored for effectiveness and any weaknesses addressed through “immediate and effective action” targeting root causes.⁸
- ▶ **Sanctions compliance programs should be tested and audited routinely. As in the AML context, organizations should have a comprehensive, independent, and objective testing or audit function to gauge the effectiveness of internal controls.**⁹ Where there are negative findings, OFAC expects “immediate and effective” remedial action.¹⁰



- ▶ **An organization’s sanctions compliance program requires sanctions-specific training. Training should be tailored for different employees and scoped to the organization’s particular products, services, clients, and geographic areas.** The frequency of training should be determined by a company’s risk profile, with resources and materials easily available to relevant personnel.¹¹

Guidance with Global Implications

OFAC “strongly encourages” anyone subject to U.S. jurisdiction to implement a sanctions compliance program. While this includes U.S. persons and other individuals and entities doing business in the United States, it also includes non-U.S. persons who use U.S.-origin goods and services. OFAC states in the guidance what has long been seen in practice through high-profile civil and criminal cases against non-U.S. persons who rely on U.S. financial institutions to perform U.S. dollar-clearing activities or who use U.S.-origin products or services in contravention of U.S. sanctions prohibitions.

In practice, this means that non-U.S. persons should have programs in place to determine if a U.S. jurisdictional nexus exists for any given transaction and, if so, to apply relevant U.S. sanctions requirements. These compliance programs are important for any person engaged in international trade, given the central role of the United States and the U.S. dollar in the global financial system and international supply chains.

OFAC’s Increasing Focus on the Adequacy of Compliance Programs

The OFAC Compliance Guidance comes amid a rapid pace of OFAC enforcement activity.¹² OFAC’s recent activity touches on a wide variety of compliance failures, including a lack of knowledge about a company’s OFAC obligations, the failure of companies’ internal controls, and intentional efforts to evade U.S. sanctions through practices such as “stripping.”¹³ These include:

- ▶ UniCredit Bank’s April 15, 2019, settlement in connection with more than 2,100 transactions processed in violation of six different OFAC sanctions programs.¹⁴ While UniCredit implemented a sanctions compliance program that included screening software and directives from in-house counsel not to process dollar-denominated transactions for Iranian parties, the bank also instituted measures to circumvent OFAC sanctions, even distributing a guidebook for employees in Europe. Circumvention measures included



stripping and asking customers to re-submit transactions to avoid OFAC regulations.

- ▶ An April 11, 2019 settlement with Acteon Group Ltd. and 2H Offshore Engineering Ltd. for seven apparent violations of the Cuban Assets Control Regulations.¹⁵ 2H Offshore, a U.S.-owned company, provided services for a well-drilling project in Cuban territorial waters. To avoid detection, 2H's senior management directed employees to strip references to Cuba from the project's documentation. As a result, Acteon, the U.S.-owned parent company, approved the deal in violation of the U.S. embargo.
- ▶ e.l.f. Cosmetics, Inc.'s January 31, 2019 settlement for 156 apparent violations of North Korean Sanctions Regulations.¹⁶ The apparent violations were 156 separate shipments of false eyelash kits from Chinese suppliers, which contained North Korean-sourced materials. Due to a "non-existent or inadequate" OFAC compliance program, e.l.f.'s supplier audits failed to identify the country of origin of the source materials being used by e.l.f.'s suppliers. In addition to a \$996,080 settlement, OFAC required e.l.f. to implement new supply chain audits addressing countries of origin of goods and services, a mandatory training program on U.S. sanctions, and engagement of outside counsel to provide additional training to key employees.
- ▶ A December 12, 2018 settlement agreement with Yantai Jereh Oilfield Services Group Co., Ltd., for 11 apparent violations of the Iranian Transactions and Sanctions Regulations.¹⁷ While the company set a general policy in 2011 not to engage in business with Iran, the company had virtually no implementing procedures, systems, or controls. Following the lifting of non-U.S. sanctions targeting Iran in 2013, the company began selling products to Iranian companies that contained U.S.-origin components. The company performed no evaluation of its exposure to U.S. sanctions.
- ▶ A November 27, 2018 settlement with Cobham Holdings, Inc. for three apparent violations of the Ukraine Related Sanctions Regulations.¹⁸ The apparent violations occurred as a result of out-of-date screening software, which failed to reflect OFAC's designation of a Cobham customer after Cobham began doing business with the by-then-designated party.

As part of its guidance, OFAC drew upon past enforcement actions to compile a list of ten common compliance program failures that often lead to OFAC penalties. Based on that list, companies should take care to do the following:

- ▶ **Have a formal OFAC sanctions compliance program.** OFAC identified that

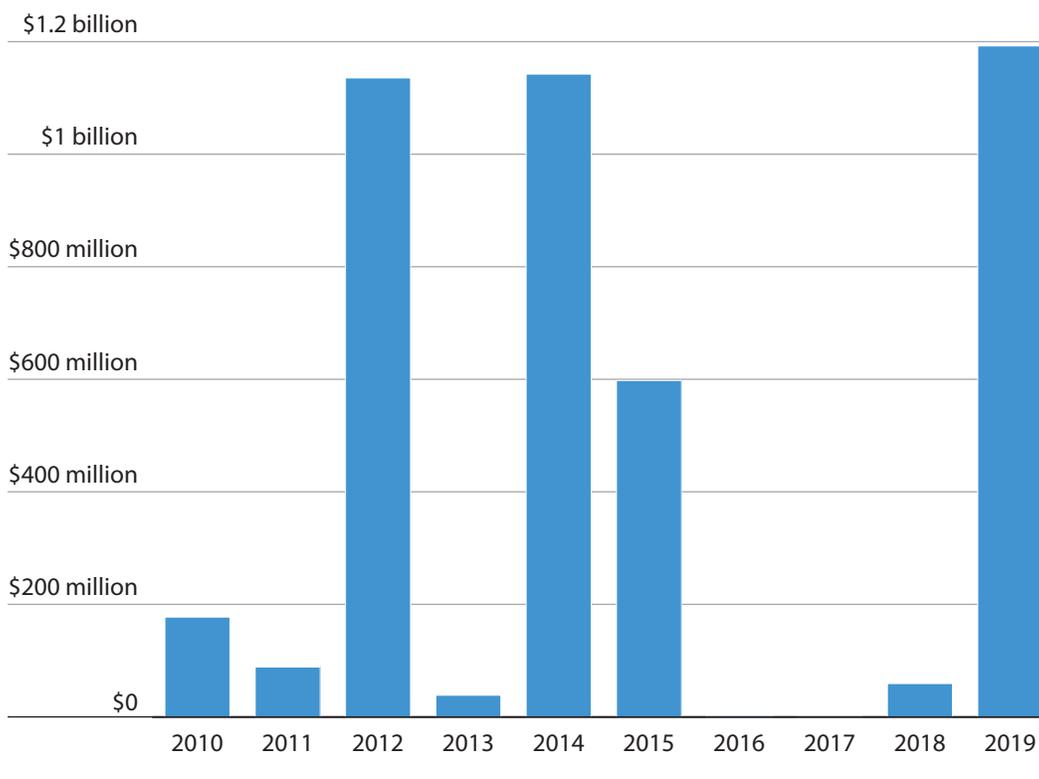


failing to implement a formal sanctions compliance program has been a root cause of sanctions violations. Lack of a program is also frequently cited as an aggravating factor, increasing the severity of penalties.¹⁹

- ▶ **Understand OFAC’s regulations and when they apply. Misinterpretation of the OFAC regulations – particularly as they relate to OFAC’s jurisdiction over non-U.S. businesses – is a root cause of OFAC violations.** Beyond missing jurisdictional nuance, these failures also lead organizations to miss warning signs of sanctioned activity and, consequently, have been treated as an aggravating factor in enforcement actions.²⁰ These failures are often attributable to a lack of training and competent compliance staff, which are noted in the OFAC guidance.
- ▶ **Ensure that international operations relying on U.S. personnel comply with OFAC regulations.** OFAC notes that multiple organizations have violated U.S. sanctions by involving U.S. persons in dealings between their

OFAC Penalties Assessed Against Financial Institutions Each Year

OFAC has assessed or agreed to nearly \$1.2 billion in penalties so far in 2019, the most ever.





non-U.S. divisions and OFAC-sanctioned parties.²¹ This often stems from a fundamental misunderstanding of the jurisdictional scope of OFAC sanctions. Organizations and their personnel should know that facilitation of sanctioned activity by a U.S. person – whether by providing transaction approvals, being part of a supply chain, or otherwise providing support – extends U.S. jurisdiction to non-U.S. operations. Recusal systems, regular training, and periodic notices to maintain awareness of U.S. regulations are all options for addressing this issue.

- ▶ **Know when products and services incorporate U.S.-origin goods, technology, or services, and ensure that exports and re-exports, to the extent relevant, comply with OFAC regulations.** Many OFAC violations have stemmed from purchases of U.S. goods with the intent to re-export the items to U.S.-sanctioned parties.²² As with operations involving U.S. persons, products and services with U.S. supply chains must be carefully reviewed.
- ▶ **Ensure that U.S. dollar-denominated transactions comply with U.S. sanctions requirements.** Dollar-denominated payments almost always require processing by a U.S. financial institution, and as a result, are subject to U.S. jurisdiction.²³ OFAC has typically taken action with respect to dollar-denominated payments that involve U.S. financial institutions when they involve repeat transactions or willful and reckless conduct. Organizations should take care to ensure that activities paid for in dollars comply with OFAC sanctions regulations.
- ▶ **Maintain current, accurate, and effective screening software. Automated systems to detect sanctioned parties are a basic element of any sanctions compliance program.** Many OFAC violations stem from failures to update systems to reflect the latest lists of designated parties, failure to account for alternative spellings of names and places (so-called “fuzzy logic” systems), or failure to incorporate pertinent identifiers.²⁴
- ▶ **Perform adequate, risk-based due diligence on outside parties. OFAC considers due diligence “fundamental” to effective compliance.** At the very least, organizations must ensure that they know who their customers and counterparties are (including their ownership), what their lines of business are, with whom they do business, and where they are located.²⁵
- ▶ **Implement a compliance program with some level of centralization and formal procedures.** De-centralized programs, with personnel holding compliance responsibilities spread out across different offices



and business units, often lead to OFAC violations due to inefficiency, miscommunication, and lack of oversight.²⁶

- ▶ **Apply industry standards to day-to-day business activities. While OFAC acknowledges that normal business activities will vary by industry, it also notes that non-traditional business practices are often used to try to evade OFAC sanctions.** Businesses should therefore follow norms and standards for their industry and may treat requests to structure transactions in unusual ways as a “red flag” for potential sanctioned activities.
- ▶ **Maintain effective oversight of individual employees. OFAC identifies several instances of insider threats – particularly at supervisory, managerial, or executive levels – defeating otherwise robust compliance programs.**²⁷ Organizations should account for the human factor by ensuring personnel and management understand individual liability for sanctions violations, performing regular compliance audits, and maintaining systems such as whistleblower hotlines.



Endnotes

- 1 Department of the Treasury Office of Foreign Assets Control, A Framework for OFAC Compliance Commitments at 1 (May 2019), available at https://www.treasury.gov/resource-center/sanctions/Documents/framework_ofac_cc.pdf. (emphasis added)
- 2 *Id.*
- 3 DOJ's guidance, for example, directs the reader to "review guidance published by relevant federal and state agencies" in cases involving complex regulatory environments. Department of Justice Criminal Division, Evaluation of Corporate Compliance Programs at 18, n 2 (April 2019), available at <https://www.justice.gov/criminal-fraud/page/file/937501/download>. U.S. sanctions compliance would likely qualify. While the FFIEC provides more specific sanctions program guidance than the DOJ, its treatment of the area largely focuses on name screening and risk assessments. See FFIEC, Bank Secrecy Act/Anti-Money Laundering Examinations Manual at 152-53 (2014), available at https://www.ffiec.gov/bsa_aml_infobase/documents/BSA_AML_Man_2014_v2.pdf (FFIEC Manual) (guidance on OFAC sanctions programs at regulated financial institutions).
- 4 OFAC Compliance Guidance at 2.
- 5 *Id.* at 3-4.
- 6 *Id.* at 4-5.
- 7 FFIEC Manual, *supra* n. 1.
- 8 OFAC Compliance Guidance at 6.
- 9 *Id.* at 6-7.
- 10 *Id.* at 7.
- 11 *Id.* at 7-8.
- 12 See, e.g., Settlement Agreement, UniCredit Bank, AG. At 13-16 (OFAC Apr. 15, 2019), https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190415_unicredit_bank_ag.pdf.
- 13 "Stripping" is the practice of removing key identifying information from wire transfer instructions in order to avoid detection by automated screening systems. Examples of stripping cases include *United States v. BNP Paribas* (S.D.N.Y. June 28, 2014) and *United States v. Standard Chartered Bank*, No. 1:12-cr-00262-JEB (D.D.C. Feb. 10, 2012).
- 14 Settlement Agreement, UniCredit Bank AG, *supra* n. 12.
- 15 Settlement Agreement, Acteon Group Ltd. (OFAC Apr. 11, 2019), https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190411_acteon_webpost.pdf.
- 16 Settlement Agreement, e.l.f. Cosmetics, Inc. (OFAC Jan. 31, 2019), https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20190131_elf.pdf.
- 17 Settlement Agreement, Yantai Jereh Oilfield Services Group Co, Ltd., ENF-46105 (OFAC Dec. 12, 2018), https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20181212_jereh_settlement.pdf.
- 18 Settlement Agreement, Cobham Holdings, Inc. (OFAC Nov. 27, 2018), https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20181127_metelics.pdf.
- 19 OFAC Compliance Guidance at 9.
- 20 *Id.*
- 21 *Id.* at 9-10.
- 22 *Id.* at 10.
- 23 *Id.*
- 24 *Id.*
- 25 See *id.* at 11.
- 26 *Id.* at 11.
- 27 *Id.* at 12.