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COMPLIANCE PROGRAMS

Important Takeaways From the National Oilwell Varco Inc. Settlement

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On November 14, the U.S. Treasury Department's Office of Foreign Assets Control (OFAC) announced a settlement with Houston-based National Oilwell Varco Inc. (''NOV'' or the ''Company'') and two of its subsidiaries related to alleged violations of the Cuban, Iranian, and Sudanese sanctions regulations. The Company entered into a concurrent settlement agreement with the Department of Commerce's Bureau of Industry and Security (BIS) and non-prosecution agreement with the U.S. Department of Justice (DOJ), agreeing to pay at least $25 million to resolve its potential liability.[1]

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This article provides an overview of the NOV settlement and highlights trends across recent sanctions- and export-related enforcement actions involving companies in the oil and gas industry.

I. Factual Background

A. Alleged Sanctions Violations

OFAC alleged that NOV and two subsidiaries, Dreco Energy Services Ltd. (Dreco) and NOV Elmar (Elmar), engaged in six categories of transactions that violated U.S. sanctions regulations. Specifically, OFAC claimed that:

- NOV approved four commission payments (with an aggregate value of $2,630,091) from Dreco to a U.K.-based entity related to the sale and exportation of goods to Iran;
- NOV engaged in (or facilitated) two sale and export transactions involving Iran, with a total value of $13,596,980;
- Dreco indirectly exported goods from the U.S. to Iran on at least seven occasions (with knowledge that the ultimate end users were Iranian customers), with a total value of $526,480;
- Dreco made 45 sales to Cuba, with a total value of $1,707,964;
- Elmar made two sales to Cuba, with a total value of $103,119; and
- NOV engaged in one export transaction involving Sudan, with a value of $20,928.

[1] OFAC issued an enforcement notice, and NOV's settlement agreement with BIS has been published online. As of this writing, the DOJ non-prosecution agreement is not publicly available.

All of these transactions occurred between 2002 and 2009, and NOV did not voluntarily disclose any of the alleged violations.

OFAC determined that the four Dreco commission payments related to transactions involving Iran were egregious sanctions violations because the payments were approved by senior-level finance executives and NOV ''willfully blinded itself to the consequences of its approval by acquiescing to Dreco's deliberate non-identification of Iran in its communications with NOV.'' OFAC also asserted that, over a three-year period, NOV ignored warning signs that approval of the commission payments violated U.S. sanctions against Iran.

OFAC calculated a base penalty of $8,537,183, which was reduced to $5,976,028 based on consideration of mitigating factors, including NOV's cooperation with OFAC's investigation and the Company's agreement to implement compliance program enhancements. The final $5,976,028 settlement amount will be deemed satisfied by NOV's payment of $25 million to DOJ under the Company's non-prosecution agreement.

B. Alleged Export Control Violations

BIS asserted a total of 22 violations of the Export Administration Regulations (EAR) by NOV and Dreco, which involved two categories of transactions.

First, BIS alleged that Dreco indirectly exported U.S.-origin oil and gas equipment via Canada to end users in Iran on 21 occasions, without obtaining a required license. According to BIS, Dreco ordered the equipment from a supplier in the U.S., without disclosing that the equipment was destined for end users in Iran. Upon receipt, Dreco allegedly transshipped the equipment from Canada to the National Iranian Drilling Co. and Kala Naft, the procurement arm of the National Iranian Oil Co. These 21 transactions occurred between April 2006 and December 2007, and the equipment at issue was valued at over $2.3 million. Because of the limited factual detail in the OFAC enforcement notice, it is unclear whether any of these 21 alleged violations overlapped with the conduct charged by OFAC.

Second, BIS alleged that in January 2012, NOV committed a single violation of the EAR when it exported controlled items to Oman in violation of an existing export license. According to the settlement agreement, NOV obtained an export license from BIS authorizing the export of nine filament winder mandrels—which are controlled for nuclear proliferation reasons—to an end user in Oman. BIS alleged that NOV exported a total of 21 filament winder mandrels to the Omani end user, without obtaining authorization for the 12 filament winder mandrels (valued at $69,615) that exceeded the Company's export license.

For the 22 alleged violations, BIS assessed a civil penalty of $2.5 million. In addition, the BIS settlement agreement provides that NOV and Dreco's export privileges may be suspended for a period of one year if (1) NOV fails to comply with the terms of its non-prosecution agreement with DOJ; or (2) either company fails to comply with the terms of the OFAC settlement.

II. Increased Scrutiny of the Oil and Gas Industry

The NOV settlement is the latest major enforcement action brought against a company operating in the oil and gas sector. In November 2013, oilfield services company Weatherford International Ltd. (Weatherford) agreed to pay $253 million in criminal and civil penalties as part of a global settlement with the DOJ, the U.S. Securities and Exchange Commission (SEC), OFAC and BIS to resolve claims that the company and its subsidiaries violated various export control laws, sanctions regulations, and the U.S. Foreign Corrupt Practices Act. Less than two years later, another oilfield services provider, Schlumberger Oilfield Holdings Ltd. (Schlumberger), pleaded guilty to violations of the International Emergency Economic Powers Act for its role in transactions involving Iran and Sudan and agreed to pay a penalty of $232.7 million.

Due to the massive penalties involved, the Weatherford and Schlumberger settlements have commanded much attention; however, these settlements are not the only recent enforcement actions targeting oil and gas companies for failing to comply with economic sanctions and export control laws. In October 2014, a subsidiary of Robbins & Myers Inc. (which, coincidentally, was acquired by NOV in 2013) agreed to pay a $1 million criminal fine and civil penalties of $600,000 after a foreign subsidiary exported stators used for oil extraction, made from U.S.-origin steel, to a customer in Syria in contravention of the EAR. More recently, in February, CGG Services SA (CGG Services) agreed to pay $614,250 to resolve alleged violations of the Cuban sanctions for (1) exporting spare parts from the United States to vessels operating in Cuban territorial waters; and (2) processing seismic data gathered in Cuba's Exclusive Economic Zone. Also in February, two subsidiaries of Halliburton Energy Services Inc. (Halliburton) agreed to pay over $300,000 to resolve alleged violations of the Cuban sanctions for exporting goods and services to an oil and gas production consortium that was five percent owned by a state-owned Cuban company. These settlements are *in addition to* recent corruption-focused investigations involving companies with ties to the oil and gas industry, including Petroleo Brasileiro SA (Petrobras), Key Energy Services Inc., Unaoil, Total SA, and many others.

Collectively, the above-described settlements suggest that the U.S. government is carefully scrutinizing oil and gas companies' compliance with sanctions regulations and export control laws, which is not surprising given these companies' heightened risk profile. In particular, oil and gas industry participants tend to have expansive international operations, including operations in countries subject to various sanctions and export controls. Further, exploration and production activities require the use of a wide variety of equipment and software, including high-tech items that have potential military applications.

III. Takeaways

A. Multi-agency Enforcement Is the New Normal

The NOV settlement is the latest in a series of high-profile enforcement actions involving more than one federal agency. In this matter, NOV was under investigation by at least three U.S. government agencies (BIS, DOJ and OFAC) and entered into separate agreements with each of those agencies.

Cooperation among federal—and, on occasion, state and international—regulators has become increasingly

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common, and multi-agency investigations present unique challenges for targeted companies. In these matters, the targeted company must respond to inquiries and allegations levied by various agencies related to purported violations of different legal regimes, which make the investigations more complicated, time-consuming, and costly to complete. In addition, multi-agency investigations can be challenging to resolve, as each investigating agency has its own enforcement policies and priorities. As multi-agency enforcement appears primed to continue, companies may find themselves under financial and operational pressure to develop strategies for managing these complex investigations.

B. A Strong Compliance Program Is Essential, and Regulators Grade on a Sliding Scale

The NOV settlement also underscores the importance of oil and gas companies implementing robust sanctions and export control compliance programs. OFAC expressly concluded that NOV's sanctions compliance program during the relevant time period was ''wholly inadequate'' given that ''NOV is a large and sophisticated company that is engaged in the business of providing oilfield services around the world, including regions with high sanctions risk.'' OFAC treated NOV's lack of an adequate compliance program as an aggravating factor when calculating the applicable penalty. OFAC has taken similar actions in other enforcement notices involving oil and gas companies.[2]

Firms in the oil and gas industry tend to be large companies with operations in many countries, and it is increasingly apparent that U.S. regulators hold sophisticated companies to a higher compliance standard. Oil and gas companies would be well-served to keep this perception in mind as they make decisions regarding the existence, nature, and scope of their sanctions and export control compliance programs.

C. Regulators Are Aggressively Pursuing Companies That Facilitate Dealings With Embargoed Countries

U.S. individuals and entities are prohibited from ''facilitating'' activities by a non-U.S. person with embargoed countries or sanctioned parties, if such activity would violate the OFAC sanctions regulations if carried out by a U.S. person. Common examples of prohibited facilitation include U.S. persons (1) approving, financing, or providing transportation or insurance for transactions involving embargoed countries; or (2) referring business opportunities involving a sanctioned party to a third party outside of the U.S.

OFAC's enforcement notice indicates that NOV violated U.S. sanctions regulations by facilitating activities related to Iran. Specifically, OFAC alleged that NOV facilitated business with Iran by approving Dreco commission payments to a foreign entity related to Dreco's direct and indirect sale of goods to Iran. OFAC concluded that this conduct constituted egregious violations of the sanctions regulations, warranting increased monetary penalties.[3] OFAC further alleged that NOV engaged in ''the direct or indirect sale and exportation of goods to Iran, and/or facilitated those transactions'' in contravention of the Iranian sanctions. The OFAC enforcement notice provides limited detail about the underlying facts, so the precise nature and scope of NOV's activities are unclear.

Recent enforcement actions suggest that OFAC and DOJ are increasingly willing to bring cases against U.S. companies—or companies with U.S. operations—that engage in facilitation. For example, the DOJ charged Schlumberger with criminally violating U.S. law by engaging in improper facilitation. Consequently, U.S.-based companies—and foreign companies with U.S. operations—should strive to ensure that U.S. entities or employees physically located in the U.S. are not involved with business involving embargoed countries or sanctioned persons.

D. A Company Can Incur Liability by Acting With 'Willful Blindness' or Having 'Reason to Know' That Transaction Involves an Embargoed Country or Sanctioned Party

OFAC's enforcement notice states that NOV ''willfully blinded itself to the consequences of its approval [of the Dreco commission payments] by acquiescing to Dreco's deliberate non-identification of Iran in its communications with NOV.'' The enforcement notice further states that ''NOV had reason to know that the commission payments involved Iran'' and ''NOV ignored several warning signs over the course of three years that approving the commission payments was prohibited conduct.''

OFAC's suggestion that missed ''warning signs'' are sufficient to incur sanctions liability is consistent with recent case law. In *Epsilon Electronics Inc. v. United States Department of the Treasury, Office of Foreign Assets Control*, 168 F. Supp. 3d 131 (D.D.C. 2016), a federal district court upheld OFAC's imposition of a $4,073,000 civil penalty on Epsilon Electronics, an automotive audio electronics company, for violating the Iranian sanctions. The court concluded that Epsilon ''had reason to know'' that a Dubai-based purchaser would resell Epsilon's products to end users in Iran for various reasons, including that the purchaser's website (1) included a contact address for an office in Iran; (2) ''touted [the purchaser's] success in the Iranian car audio and video market''; (3) ''listed dealers located exclusively in Iran''; and (4) ''displayed photographs of what appeared to be car shows in various Iranian cities.''[4]

The NOV settlement and *Epsilon Electronics* decision illustrate that an individual or entity is not required to

[2] *See* OFAC Enforcement Information, Dep't of Treasury, Halliburton Atlantic Limited and Halliburton Overseas Limited Settle Potential Civil Liability for Alleged Violations of the Cuban Assets Control Regulations (Feb. 25, 2016) (''Halliburton and its affiliated companies are sophisticated entities that regularly deal in oilfield goods and services around the world . . . [and] Halliburton's sanctions compliance program was inadequate because it did not include a procedure to screen all of the Consortium members.''); OFAC Enforcement Information, Dep't of Treasury, Weatherford International Ltd. Settles Potential Civil Liability for Apparent Violations of Multiple Sanctions Programs (Nov. 26, 2013) (''Weatherford is a large and sophisticated oilfield services company . . . and Weatherford's compliance program at the time of the apparent violations was substantially deficient.'').

[3] The Dreco commission payments were the only NOV violations that OFAC determined to be egregious.

[4] *Epsilon Elecs. Inc.*, 168 F. Supp. 3d at 140-41.

have actual knowledge it is violating the law in order to incur sanctions liability. Merely having reason to know of potential sanctions violations—or consciously disregarding the possibility—can be enough for a U.S. person to violate the sanctions regulations.

E. The Wheels of Justice Turn Slowly

The NOV settlement highlights another common trend in sanctions and export control enforcement actions: BIS and OFAC take their time investigating and resolving these matters. NOV's relevant conduct spanned from 2002 to 2009,[5] but BIS and OFAC (as well as DOJ) did not resolve the matter until late 2016. It is unclear why BIS and OFAC have been slow to resolve cases involving older conduct (e.g., the 2016 Halliburton settlement involved conduct from 2011; the 2016 CGG Services settlement involved conduct from 2010-11; the 2014 Robbins & Myers settlement involved conduct from 2006). In the case of OFAC, it is possible that the agency's investigative efforts have been hampered by resource constraints or recent employee turnover. Whatever the reasons, BIS and OFAC may have pipelines of active enforcement matters involving more recent conduct that are progressing towards resolution.

A related trend is the willingness of companies under investigation to toll the applicable statute of limitations. NOV agreed to toll the statute of limitations for over seven years to allow OFAC to complete its investigation. NOV almost certainly entered into a tolling agreement with BIS, too, as all but one of the alleged violations occurred from 2006-07. Other companies recently investigated by OFAC also agreed to toll the statute of limitations for extended periods of time. Increasingly, U.S. regulators seem to expect companies to toll the statute of limitations in order to obtain maximum cooperation credit.

[5] One violation alleged by BIS occurred in 2012.

F. Sanctions and Export Control Violations Rarely Occur in Isolation

OFAC alleged that NOV engaged in six categories of transactions that violate U.S. sanctions against three countries (Cuba, Iran, Sudan). Similarly, the violations charged by BIS involved two unrelated schemes and multiple countries (Iran, Oman). Other recent settlements involving oil and gas companies also have involved conduct in multiple countries, including Weatherford (Cuba, Iran, Sudan) and Schlumberger (Iran, Sudan). And although they each involved only one country, the Robbins & Myers, CGG Services, and Halliburton settlements were based on multiple violations. Succinctly put, when a company discovers a single sanctions or export control violation, further investigation is likely to uncover other, additional violations. Similarly, when a company discovers a violation involving one country, there is a strong possibility that the company engaged in impermissible conduct involving other countries as well.

IV. Conclusion

Aggressive enforcement of oil and gas companies for sanctions and export control violations is likely to continue, at least until companies respond by implementing robust compliance procedures. As the settlements discussed above demonstrate, an upfront investment in compliance enhancements may be worthwhile to avoid potential violations and stave off government investigations down the road.

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