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# OFAC Raises the Compliance Bar: Takeaways from the Stanley Black & Decker Settlement

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On March 27, the Office of Foreign Assets Control ("OFAC") announced a $1.869 million settlement with Stanley Black & Decker, Inc. ("SB&D") and its Chinese subsidiary, Jiangsu Guoqiang Tools Co., Ltd. ("GQ," and collectively with SB&D, the "Company"), to resolve 23 apparent violations of the Iranian Transactions and Sanctions Regulations ("ITSR").[1] In addition to a civil penalty, the settlement imposes extensive sanctions compliance commitments on the Company, backed by a five-year annual certification requirement.

While the SB&D settlement does not represent a significant financial penalty in comparison to other recent actions, it is the most recent in a series of enforcement actions through which OFAC appears to be communicating, in uncharacteristically direct terms, heightened compliance expectations of companies subject to its jurisdiction. This messaging is reflected in the 26 specific compliance commitments that SB&D agreed to undertake as part of the overall settlement. The settlement also makes explicit that acquiring firms' sanctions-focused diligence obligations extend ***beyond*** closing. In particular, where an investment target has known, historical dealings with sanctioned countries, reliance upon clear instructions against sanctioned country transactions, written sanctions policies and procedures, and employee training may not be sufficient.

## SB&D Settlement

### *Factual Background*

In 2011, SB&D began exploring a potential acquisition of GQ, a China-based manufacturer and distributor of power tools.[2] SB&D conducted pre-acquisition due diligence of GQ, which found that GQ exported products to Iran.[3] As a condition to closing, SB&D required GQ to terminate its sales to Iran (as well as other sanctioned countries), and GQ's senior management signed written agreements "in which they attested that GQ would not engage in transactions with Iran."[4] In May 2013, upon completing a 60% investment in GQ, SB&D (1) "provided a series of trainings to GQ employees on the company's policies and procedures as they related to OFAC's sanctions programs"; and (2) reviewed SB&D's trade compliance policies and procedures with members of GQ's export team.[5]

Notwithstanding SB&D's pre- and post-investment compliance efforts, GQ continued to export products to Iran through December 2014.[6] Upon learning of these transactions, SB&D initiated an internal investigation, which determined that

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[1] Settlement Agreement between the U.S. Department of the Treasury's Office of Foreign Assets Control and Stanley Black & Decker, Inc. and Jiangsu Guoqiang Tools Co., Ltd. (Mar. 27, 2019), [hereinafter, "SB&D Settlement"].
[2] *Id*. at 1.
[3] *Id*. at 1-2.
[4] *Id.* at 2.
[5] *Id*. at 1-2; OFAC, Stanley Black & Decker, Inc. Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations Committed by Its Chinese-Based Subsidiary Jiangsu Guoqiang Tools Co. Ltd. (Mar. 27, 2019), [hereinafter, "SB&D Enforcement Information"], at 1. Although non-U.S. entities generally are not required to comply with U.S. sanctions, the prohibitions of the ITSR apply to non-U.S. entities that are majority-owned by U.S. entities.
[6] SB&D Settlement at 2-3.

GQ employees concealed the Iranian transactions by (1) exporting products to Iran via trading companies located in China and the United Arab Emirates; (2) creating fictitious shipping documents; and (3) instructing customers to omit references to Iran from business documents.[7] The investigation found that "various GQ board members and senior management participated in these activities with knowledge that such conduct violated its parent company's policies and U.S. economic sanctions against Iran."[8]

Between June 29, 2013 and December 30, 2014, GQ exported, or attempted to export, 23 shipments of power tools and spare parts to Iran, with a total value of $3,201,647.73, in apparent violation of the ITSR.[9] SB&D voluntarily disclosed the apparent violations to OFAC on behalf of GQ.[10]

***Settlement & Compliance Undertakings***

OFAC determined that the apparent violations of the ITSR constituted an egregious case, and calculated a statutory maximum civil penalty of $6,922,757 and base civil penalty of $3,461,378.[11]

Pursuant to the settlement agreement, the Company is required to pay a civil penalty of $1,869,144.[12] In addition, the agreement sets out 26 specific compliance commitments, including:

- Commitment to refrain from employing, directly or indirectly, the managers responsible for, and involved in, the apparent violations;
- Requirement to conduct a periodic, OFAC-focused risk assessment;
- Requirement to communicate the Company's sanctions compliance policies and procedures to all relevant staff, including personnel within the sanctions compliance function, as well as relevant gatekeepers and business units operating in high-risk areas (*e.g.*, customer acquisition, payments, sales, etc.);
- Requirement to update the Company's risk assessment and review its sanctions policies, procedures, and practices on a periodic basis in order to identify and correct any weaknesses or deficiencies;
- Requirement to provide OFAC-related training, at a minimum, at least once a year to all relevant employees; and
- Requirement to ensure that the Company's OFAC-related training program provides adequate information and instruction to employees and stakeholders (for example, clients, suppliers, business partners, and counterparties).[13]

Within 180 days, the Company must submit to OFAC an interim progress report on the implementation of the 26 compliance commitments set out in the settlement agreement.[14] In addition, for a five-year period, the Company will be required to submit annual certifications to OFAC "confirming that [the Company] has implemented and continued to maintain" the compliance commitments imposed under the settlement agreement.[15]

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[7] *Id*.
[8] *Id*. at 2.
[9] *Id*. at 3.
[10] SB&D Enforcement Information at 1.
[11] *Id*.
[12] SB&D Settlement at 4.
[13] *Id*. at 4-8.
[14] *Id*. at 8.
[15] *Id*.

## Key Takeaways

***OFAC Expects Investors to Conduct Both Pre-Acquisition Diligence & Post-Acquisition Monitoring***

SB&D conducted pre-acquisition due diligence of GQ, which was sufficient to identify GQ's Iran-related business dealings. The settlement agreement states that SB&D "took steps to cease GQ's sales to, and transactions with, Iran and other OFAC-sanctioned countries prior to the acquisition date and made ceasing such sales a pre-requisite condition of the closing."[16] In addition, after closing, SB&D took steps to incorporate GQ into SB&D's existing sanctions compliance program, including by reviewing policies with—and providing training to—relevant GQ personnel.[17]

Despite these steps, OFAC faulted SB&D for failing to "implement procedures to monitor or audit GQ's operations to ensure that its Iran-related sales had in fact ceased or did not recur post-acquisition."[18] In doing so, OFAC appears to be communicating that pre-acquisition due diligence, negotiation of a condition precedent to terminate sanctioned country sales, and post-closing policy adoption and training are necessary, but not sufficient, steps when a U.S. firm acquires a non-U.S. target with sanctioned country dealings. In the accompanying enforcement information, OFAC observed that the settlement "highlights the importance for U.S. companies to conduct sanctions-related due diligence both prior and subsequent to mergers and acquisitions, ***and to take appropriate steps to audit, monitor, and verify newly acquired subsidiaries and affiliates for OFAC compliance***."[19]

OFAC made a similar observation approximately one month ago, in connection with a $5.5 million enforcement action against German chemical manufacturer AppliChem GmbH. ("AppliChem").[20] U.S.-based Illinois Tool Works, Inc. ("ITW") acquired AppliChem in January 2012.[21] Prior to closing, ITW instructed AppliChem that the company would need to terminate its Cuba-related business upon completion of the transaction.[22] Shortly after closing, ITW circulated to AppliChem's managers a memorandum summarizing ITW's sanctions compliance guidelines.[23] Despite these steps, AppliChem continued to engage in transactions with Cuban counterparties.[24] ITW submitted a voluntary disclosure to OFAC on behalf of AppliChem in January 2013, representing that AppliChem had terminated its remaining Cuba-related business, and OFAC issued a cautionary letter to ITW in May 2015.[25]

Even after receipt of the cautionary letter, AppliChem continued to conduct business with Cuba, and its employees took steps to conceal these transactions from ITW personnel.[26] Upon discovering the ongoing Cuba-related activity, ITW conducted an internal investigation and submitted a second voluntary disclosure to OFAC.[27] Although it ultimately elected to impose a monetary penalty against AppliChem (as opposed to the parent entity, ITW), OFAC observed that the "case demonstrate[d] the importance of . . . performing follow-up due diligence on acquisitions of foreign persons known to engage in historical transactions with sanctioned persons and jurisdictions.").[28]

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[16] *Id*. at 1.
[17] *Id*. at 1-2.
[18] *Id*. at 2.
[19] SB&D Enforcement Information at 3 (emphasis added).
[20] OFAC, AppliChem GmbH Assessed a Penalty for Violating the Cuban Assets Control Regulations (Feb. 14, 2019).
[21] *Id*. at 1.
[22] *Id*.
[23] *Id*.
[24] *Id*.
[25] *Id*.
[26] *Id*. at 1-2.
[27] *Id*. at 2.
[28] *Id*. at 3.

Following the SB&D and AppliChem actions, U.S. firms that acquire or make significant investments in non-U.S. companies with known sanctioned party or country dealings are firmly on notice that OFAC expects acquirers to supplement pre-acquisition diligence with robust post-acquisition monitoring, to ensure that acquired companies have established appropriate compliance controls and are, in fact, complying with U.S. sanctions.

***U.S. Firms Are Responsible for the Actions of Their Foreign Affiliates***

Along similar lines, the SB&D settlement is a reminder that U.S. firms may be held liable for the actions of their foreign affiliates, even where U.S. personnel were not aware of, and did not participate in or facilitate, the underlying transactions.

According to the settlement agreement, GQ "engaged in non-routine business practices in order to conceal and facilitate GQ's prohibited exports to Iran."[29] OFAC determined that GQ's continued dealings with Iran constituted egregious violations of the ITSR, despite the fact that SB&D (1) took steps to ensure GQ did not conduct business with Iran; and (2) voluntarily disclosed the Iran-related transactions. In addition, neither the settlement agreement nor accompanying enforcement information alleges that SB&D personnel were aware of the underlying transactions. However, because U.S. sanctions are a strict liability regime, SB&D's good intentions and lack of involvement or knowledge were not sufficient to avoid the imposition of a significant monetary penalty and extensive compliance undertakings.

In this respect, the SB&D settlement is consistent with OFAC's posture in recent enforcement actions. In February 2019, OFAC imposed a $13,381 penalty against Kollmorgen Corporation ("Kollmorgen"), based on apparent ITSR violations committed by its Turkish affiliate, Elsim Elektroteknik Sistemler Sanayi ve Ticaret Anonim Sirketi ("Elsim").[30] Like SB&D, Kollmorgen conducted pre-acquisition due diligence of Elsim, which identified historical dealings with Iran.[31] Kollmorgen proceeded to implement "a wide range of pre- and post-acquisition compliance measures designed to ensure Elsim complied with U.S. sanctions," which appear to have ***exceeded*** the compliance efforts undertaken by SB&D.[32] Among other steps, Kollmorgen (1) conducted a comprehensive review of Elsim's customer database to identify any sales or customers located in, or with connections to, countries or regions subject to U.S. sanctions; (2) performed proactive, recurring reviews of Elsim's customer database to identify any sanctions-related customers; and (3) required Elsim's senior management to certify, on a quarterly basis, that no products or services were being sent or provided to Iran.[33] Despite "Kollmorgen's extensive efforts to ensure Elsim complied with the ITSR," Elsim continued to engage in Iran-related transactions and took steps to conceal the transactions from Kollmorgen personnel.[34] OFAC concluded that the imposition of a monetary penalty, representing almost twice the base penalty amount, "was the appropriate administrative response," despite Kollmorgen's submission of a voluntary disclosure and its "extensive compliance efforts" both pre- and post- acquisition.[35]

The SB&D and Kollmorgen enforcement actions set a high bar with respect to U.S. firms' obligation to monitor their foreign affiliates' activities, and illustrate that U.S. firms may be hit with civil penalties even where foreign affiliates have purposefully circumvented existing sanctions controls. OFAC's willingness to pursue U.S. firms for the conduct of

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[29] SB&D Settlement at 2.

[30] OFAC, Kollmorgen Corporation Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations (Feb. 7, 2019), at 1.

[31] *Id.*

[32] *Id.*

[33] *Id.* at 1-2.

[34] *Id.* at 2.

[35] *Id.* at 3.

foreign affiliates presents a particular challenge for institutional investors that may have limited ability to control the day-to-day operations of the companies in which they invest.

***New Compliance Program Expectations?***

In contrast to other U.S. regulators, OFAC historically has declined to articulate minimum sanctions compliance program expectations, instead encouraging U.S. firms to adopt a "risk-based" compliance strategy that accounts for the firm's business model and industry. For example, OFAC has stated:

- "OFAC's regulations do not explicitly require any specific screening regime. Financial institutions and others must make screening choices based on their circumstances and compliance approach."[36]

- "Persons including technology companies; administrators, exchangers, and users of digital currencies; and other payment processors should develop a tailored, risk-based compliance program, which generally should include sanctions list screening and other appropriate measures. An adequate compliance solution will depend on a variety of factors, including the type of business involved. There is no single compliance program or solution suitable for every circumstance."[37]

The U.S. Treasury Department's Economic Sanctions Enforcement Guidelines similarly provide that, in assessing the appropriate administrative response to a violation of the sanctions regulations, OFAC will take into account "the existence, nature and adequacy of a Subject Person's risk-based OFAC compliance program at the time of the apparent violation, where relevant."[38]

However, in recent actions, OFAC appears be providing more detailed guidance regarding both (1) its compliance expectations; and (2) key takeaways from the individual enforcement actions. The 26 compliance commitments spelled out in the SB&D settlement—which facially are similar to the compliance undertakings that the Department of Justice routinely incorporates into deferred prosecution agreements—may represent the most complete (albeit non-comprehensive) expression of a sanctions compliance program that OFAC has published to date.

It remains to be seen if the SB&D settlement and other recent enforcement actions are a precursor to OFAC's publication of formal sanctions compliance program guidance. Regardless, the guidance provided in OFAC's recent enforcement notices suggests a more expansive view of what constitutes an adequate sanctions compliance program. By making its expectations more explicit, OFAC artfully has accorded itself greater leverage to seek monetary penalties in cases where companies' compliance efforts do not meet the steps taken by the targets of published enforcement actions.

## Conclusion

The SB&D settlement is the most recent indicator that OFAC is seeking to raise the compliance bar for U.S. firms, particularly those acquiring or investing in non-U.S. companies. As OFAC's compliance expectations have become more rigorous, they simultaneously are becoming more explicit. U.S. firms therefore would be advised to intensify their sanctions compliance efforts, particularly with respect to their foreign affiliates and acquisition targets, to ensure that their existing sanctions compliance frameworks are not falling behind evolving regulatory expectations.

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[36] OFAC, Frequently Asked Questions #124, available here.
[37] OFAC, Frequently Asked Questions #560, available here.
[38] Economic Sanctions Enforcement Guidelines, 74 Fed. Reg. 57593, 57603 (Nov. 9, 2009).