ExxonMobil Sanctions Penalty: Lessons for Companies and Practitioners

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On July 20, 2017, the U.S. Department of Treasury's Office of Foreign Assets Controls (OFAC) assessed a $2 million penalty against U.S. oil conglomerate ExxonMobil for its violation of U.S. trade sanctions on Russia enacted in response to Russia's 2014 intervention in Ukraine (the Russia-Ukraine sanctions). The penalty was assessed because of ExxonMobil's dealings with a sanctioned officer of a Russian company, even though the company itself was not subject to these sanctions. ExxonMobil is challenging the assessment, and has filed suit to have the penalty set aside.

The assessment illustrates two important lessons for companies and practitioners:

(1) Conduct diligence and get representations and covenants not only from counterparty companies, but also the company's officers and directors.

(2) Exercise caution in relying on informal guidance in dealing with sanctions.

Russia-Ukraine Sanctions

In March 2014, OFAC enacted a new U.S. sanctions regime in response to Russia's military intervention in Ukraine. The sanctions designated certain individuals (mostly those loosely affiliated with President Vladimir Putin or his administration) as "specially designated nationals" (SDNs), which broadly prohibited U.S. persons from dealing with these SDNs.

In April 2014, as part of the Russia-Ukraine sanctions program, OFAC designated Rosneft, a state-owned Russian oil company, as subject to limited sectoral sanctions that generally prohibited U.S. persons from providing financing to Rosneft or engaging in certain transactions with Rosneft relating to Arctic offshore, deepwater or shale oil. OFAC also designated Igor Sechin, CEO of Rosneft, as an SDN.

Transactions at Issue

In May 2014, after the Russia-Ukraine sanctions had been implemented and Rosneft and Sechin had been designated, officers of ExxonMobil and Rosneft signed eight legal documents related to oil and gas projects in Russia. As described in ExxonMobil's complaint (see below), the documents related to pre-existing business relationships that ExxonMobil had had with Rosneft. Seven of the documents memorialized the completion of certain conditions precedent related to joint projects in the Arctic, and the eighth memorialized the extension of a pre-existing agreement related to natural gas development in the Russian Far East.

The documents were signed by officers of ExxonMobil and by Sechin on behalf of Rosneft.

OFAC's Assessment of Penalties

The Russia-Ukraine sanctions prohibit a U.S. person from having any dealings in property of an SDN. The related OFAC regulations define "property" broadly to include services. OFAC determined that Sechin's signing of the documents constituted a service, and that ExxonMobil had "dealt in" such services in violation of the sanctions. OFAC rejected ExxonMobil's argument that Sechin's actions were taken in his professional capacity as CEO of Rosneft, and not in his personal capacity, claiming that no such distinction was made in the regulations. OFAC also cited a frequently asked question relating to the Burma/Myanmar sanctions program (which has since been repealed) in which OFAC advised that a contract with a non-prohibited entity that is signed by an SDN may result in a violation. OFAC dismissed contemporaneous informal government guidance cited by ExxonMobil suggesting that the transaction would not be prohibited.

Interestingly, OFAC did not cite two additional frequently asked questions (FAQs #398 and 400), which make very clear its view that receiving a signed contract and engaging in other business transactions with an SDN working on behalf of a non-sanctioned entity is prohibited. These FAQs were probably not cited because they were issued in August 2014, and therefore were not available when the ExxonMobil transactions at issue occurred.

The maximum statutory civil penalty for a U.S. sanctions violations is equal to the greater of $250,000 and twice the amount of the transaction that is the basis of the violation (50 U.S.C. §1705). It is unclear how the "amount" of the transactions at issue would be calculated, so presumably the $2 million penalty was calculated by multiplying $250,000 by the eight documents. OFAC determined that the violation was egregious with aggravating factors, and therefore did not reduce the maximum penalty amount.

ExxonMobil's Response

On the same day that OFAC issued its assessment, ExxonMobil filed suit in U.S. federal district court for the Northern District of Texas, seeking to have the assessment set aside. ExxonMobil cited several government statements released in conjunction with the Russia-Ukraine sanctions, arguing that the sanctions against Sechin and the other SDNs were intended to target their personal wealth and not their business actions, and applied to Sechin only in his individual capacity. ExxonMobil further argued that Sechin's "services" in signing the documents were to his employer Rosneft, not to ExxonMobil. Finally, ExxonMobil argued that the Burma/Myanmar frequently asked question did not apply, as it related to a separate sanctions program.

Political and Business Contexts

The ExxonMobil case cannot be separated from its political and business contexts. At the time of the transactions at issue, the CEO of ExxonMobil was Rex Tillerson, current U.S. Secretary of State under President Donald Trump. Tillerson was a friend of Sechin, and vocally opposed the sanctions when they were enacted (he has recused himself from the current matter, and OFAC's position is effectively represented by U.S. Secretary of Treasury Steven Mnuchin). Furthermore, Congress has passed a bill expanding and strengthening the existing Russia-Ukraine sanctions, which was signed into law by President Trump on Aug. 2, 2017 (H.R.3364—Countering America's Adversaries Through Sanctions Act). Nevertheless, ExxonMobil's complaint makes clear that OFAC's determinations in this case were formulated, in part, during the administration of former President Barack Obama, so it appears that the case is not just about politics.

Also of interest is the amount at issue. For a company as large as ExxonMobil, $2 million is a relatively small figure, and one might expect it to settle with OFAC rather than litigating. However, ExxonMobil may wish to establish a precedent giving it the unfettered right to deal with Rosneft and other non-SDN companies without worrying about violating sanctions.

Lesson #1

Importance of diligence, representations and covenants. While the ExxonMobil case is somewhat unique owing to the political and business contexts, it contains an important lesson regarding dealings with non-sanctioned entities whose directors or officers are SDNs.

Parties entering into cross-border transactions such as loans, leases and joint ventures often perform basic due diligence to confirm that their counterparties are not subject to sanctions. Contracts also frequently include a representation that the counterparty companies are not subject to sanctions, and a provision permitting the contract to be terminated if the company becomes sanctioned.

ExxonMobil confirmed (and OFAC did not dispute) that its transactions with Rosneft were not prohibited. However, it did not confirm that the officer it was dealing with was not an SDN. It is unclear from the record whether ExxonMobil knew who would be signing for Rosneft, so we do not know if ExxonMobil could have avoided sanctions if another officer had signed. But it is worth examining what protective measures companies can take to minimize their risks.

Before commencing any new transaction with a company counterpart, U.S. persons and others who wish to comply with U.S. sanctions should perform a search of both the company's name and its officers and directors, confirming that none of them are subject to sanctions. Then, in negotiating the agreement, the parties should include representations and covenants designed to prevent prohibited transactions with officers or directors that are SDNs. The agreement may include representations that none of the officers or directors of the counterparty (and potentially its subsidiaries and/or affiliates) are sanctioned persons. It may be more difficult to negotiate covenants that no such directors or officers will become sanctioned persons, since this is often beyond the parties' control. At the very least, parties may include a notification obligation if any directors or officers become sanctioned persons, so that they can exercise caution going forward.

Lesson #2

Reliance on informal guidance and administrative intent. Another useful lesson that the ExxonMobil case illustrates is parties' limited ability to rely on informal guidance and administrative intent in interpreting sanctions. In its complaint, ExxonMobil cited numerous verbal and written statements by Obama administration officials in support of its contentions that the Russia-Ukraine sanctions should be narrowly construed, were intended to target the personal assets of the listed individuals, not the companies they manage, and would not impede the ability of U.S. persons to do business with Rosneft. OFAC was apparently unmoved by these arguments, even going so far as to call ExxonMobil's actions "egregious," rather than good faith reliance on government statements. OFAC's position makes clear that it looks to regulations and formal guidance, rather than informal statements, in interpreting sanctions. Parties should therefore exercise caution in relying on any such informal guidance in the face of contrary official regulations or interpretations.

Conclusion

It remains to be seen how the ExxonMobil case will turn out. Nevertheless, parties that wish to avoid being subject to similar proceedings should carefully monitor their transactions with directors and officers of a non-sanctioned counterparty and should limit their reliance on informal guidance.

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