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In Unprecedented Move, OFAC Takes Enforcement Action Against U.S. Parent Company for Turkish Subsidiary's Iran Sanctions Violations and Simultaneously Sanctions the Subsidiary's Ex-Managing Director

Simultaneous Enforcement Action and Sanctions Designation Reflects Trump Administration's Aggressive Stance on Iran Sanctions

On February 7, 2019, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") announced a \$13,381 settlement agreement with Virginia-based Kollmorgen Corporation ("Kollmorgen"), a technology and manufacturing company, regarding six apparent violations of OFAC's Iran sanctions regulations.¹ OFAC determined that Kollmorgen's Turkish subsidiary, Elsim Elektrotechnik ("Elsim"), serviced machines located in Iran and knowingly provided products, parts, or services to Iranian end-users.² Under U.S. law, non-U.S. companies owned or controlled by U.S. companies are required to adhere to the embargo on Iran as if they were U.S. persons. Simultaneously, OFAC designated Evren Kayakiran ("Kayakiran"), the former Elsim managing director whom OFAC determined to be primarily responsible for directing the apparent violations and seeking to conceal them, as a foreign sanctions evader and added his name to the Foreign Sanctions Evaders List, thereby broadly cutting off his access to the U.S. economy.

This marks the first time that OFAC has concurrently designated a foreign sanctions evader and announced a related settlement with a U.S. company. The settlement signals the Trump Administration's willingness to hold U.S. parent companies liable for their subsidiaries' Iran sanctions violations, which is an area that has seen little enforcement activity to date. The concurrent sanctioning of Elsim's former managing director highlights increased personal risk for non-U.S. personnel that violate U.S. sanctions.

Kollmorgen's Acquisition-Related Due Diligence

According to OFAC, Kollmorgen acquired control of Elsim in early 2013, thereby subjecting Elsim to the Iranian Transactions and Sanctions Regulations (the "ITSR").³ OFAC stated that, prior to the acquisition, Kollmorgen hired outside counsel and an auditing and consulting firm to perform sanctions due diligence on Elsim, which revealed that Elsim had existing business with Iranian customers.

OFAC noted that Kollmorgen "subsequently implemented a wide-range of pre- and post-acquisition compliance measures designed to ensure Elsim complied with U.S. sanctions," including:

- “[C]onducting a comprehensive review of Elsim’s customer database in order to identify any sales to or customers located in jurisdictions subject to comprehensive U.S. economic sanctions;”
- “[I]dentifying Elsim’s Iran-related customers and applying controls to block those customers from making future orders;”
- “[D]rafting and circulating a memorandum to all Elsim employees notifying them of U.S. economic sanctions targeting Iran and their obligation to comply with [such sanctions];”
- “[C]onducting in-person U.S. sanctions compliance trainings for Elsim employees regarding Kollmorgen’s existing trade compliance policies (specifically including Iran), which included a requirement that employees promptly report any and all violations of law;”
- “[O]n a proactive and continuing basis, performing additional manual reviews of Elsim’s customer database to identify any sanctions-related customers;”
- “[R]equiring Elsim customers to agree to modified terms and conditions of sale prohibiting the resale of Elsim products, directly or indirectly to Iran;”
- “[R]equiring Elsim’s senior management to certify, on a quarterly basis, that no Elsim products or services were being sent or provided to Iran;”
- “[O]rdering Elsim’s senior management to immediately cease transactions with Iran, including any technical support;” and
- “[I]mplementing an ethics hotline for reporting violations of law.”⁴

The Apparent Violations

OFAC determined that Elsim appeared to have violated § 560.215(a) of the ITSR when it provided parts and services to Iran between July 2013 and July 2015.⁵ Section 560.215 of the ITSR implements § 218 of the Iran Threat Reduction and Syria Human Rights Act, which extends the prohibitions in the ITSR to non-U.S. companies owned or controlled by U.S. companies and imposes liability on U.S. companies for Iran sanctions violations by non-U.S. companies they own or control. The total value of the parts and services was \$14,867.

According to OFAC, in spite of Kollmorgen’s pre- and post-acquisition compliance measures, Elsim willfully, and with full knowledge of the applicable sanctions prohibitions, dispatched employees to Iran to fulfill service agreements and other transactions related to Iran.⁶ OFAC stated that Elsim management threatened to fire employees if they refused to travel to Iran and directed employees to falsify corporate

records regarding the travel to Iran. According to OFAC, Elsim management also “regularly and fraudulently” certified to Kollmorgen that no Elsim products or services were being provided to Iran.⁷

OFAC determined that Kollmorgen only learned of the apparent violations when an Elsim employee raised concerns via Kollmorgen’s corporate ethics hotline. According to OFAC, Elsim management then attempted to obstruct Kollmorgen’s internal investigation, including by deleting emails and instructing the destruction of corporate records.

OFAC indicated that Kollmorgen was nevertheless able to submit a “comprehensive report” to OFAC describing the apparent violations.⁸

Factors Affecting OFAC’s Penalty Determination

OFAC determined that Kollmorgen voluntarily self-disclosed the apparent violations and that the apparent violations constituted a non-egregious case. The statutory maximum civil monetary penalty amount for the apparent violations was \$1,500,000 and the base penalty amount was \$7,434. The settlement amount reflected OFAC’s consideration of the following facts and circumstances pursuant to OFAC’s Economic Sanctions Enforcement Guidelines.⁹

OFAC determined the following to be aggravating factors:

- “Elsim willfully provided goods and services to Iran in violation of the ITSR;”
- “Elsim management knew its employees were traveling to Iran to provide services and directed them to do so;”
- “Elsim management concealed the [a]pparent [v]iolations from Kollmorgen and others by deleting and falsifying records as well as directing their subordinates to do so;” and
- “[T]he [a]pparent [v]iolations conferred economic benefit to Iran.”¹⁰

OFAC determined the following to be mitigating factors:

- “[N]either Kollmorgen nor Elsim have received a penalty notice or finding of violation from OFAC in the five years preceding the earliest apparent violation;”
- “Kollmorgen cooperated with OFAC by conducting an effective and extensive internal investigation and submitting a comprehensive voluntary self-disclosure to OFAC;” and
- “Kollmorgen’s extensive preventative and remedial conduct.”¹¹

As is its standard practice, OFAC did not disclose how it weighed these aggravating and mitigating factors in reaching the settlement amount. OFAC also described several remedial measures undertaken by Kollmorgen to minimize the risk of future violations:

- “[T]erminating the Elsim managers responsible for, and involved in, the [a]pparent [v]iolations;”
- “[I]mplementing new procedures to educate Elsim employees on compliance with U.S. economic and trade sanctions;”
- “[R]equiring Elsim to seek pre-approval from an officer based outside of Turkey for all foreign after-sales service trips;” and
- “[R]equiring Elsim to inform its major Turkish customers that Elsim cannot provide goods or services to Iran.”¹²

Designation of Former Elsim Managing Director as a Foreign Sanctions Evader

For the first time in the context of a civil enforcement action, OFAC sanctioned an individual, Kayakiran, a Turkish national and the former Elsim managing director determined by OFAC to be “primarily responsible” for the conduct that led to the apparent violations. The designation was made pursuant to E.O. 13608, “Prohibiting Certain Transactions With Respect to Iran and Syria,” which authorizes OFAC to sanction any non-U.S. person determined to have violated, attempted to violate, conspired to violate, or caused a violation of the ITSR. Transactions by U.S. persons or within the United States involving persons or entities designated as a Foreign Sanctions Evader are prohibited, effectively cutting off any listed person or entity from the U.S. economy. Unlike designations on OFAC’s Specially Designated Nationals and Blocked Persons List, however, designation as a Foreign Sanctions Evader does not require U.S. persons to block the Foreign Sanctions Evader’s property or interests in property that are located in the United States or otherwise come under the possession or control of a U.S. person.

Sigal Mandelker, U.S. Treasury Under Secretary for Terrorism and Financial Intelligence, described the decision to sanction Kayakiran as follows:

Treasury is sanctioning Kayakiran not just for his willful violation of U.S. sanctions on Iran, but also for directing staff to commit and cover up these illegal acts. This is the first time that OFAC has designated an individual as a Foreign Sanctions Evader while resolving an enforcement matter, *and is a marked change to how we will counter these acts of deception. This action is a clear warning that anyone in supervisory or managerial positions who directs staff to provide services, falsify records, commit fraud, or obstruct an investigation into sanctions violations exposes themselves to serious personal risk.*¹³

Under Secretary Mandelker’s statement shows an increased personal risk of sanctions designations for any non-U.S. persons in managerial roles who knowingly engage in conduct in violation of U.S. sanctions.

Implications

OFAC's actions reflect the Trump administration's aggressive stance on Iran sanctions. The settlement with Kollmorgen may signal heightened OFAC interest in pursuing U.S. companies for the Iran sanctions violations of the non-U.S. companies they own or control. Additionally, OFAC's unprecedented foreign sanctions evader designation indicates heightened personal risk for non-U.S. individuals, including employees of non-U.S. subsidiaries of U.S. companies, who knowingly violate, attempt to violate, conspire to violate, or cause violations of U.S. sanctions against Iran.

The Kollmorgen settlement makes clear that OFAC expects the immediate adoption and implementation of appropriate controls when U.S. companies acquire non-U.S. companies with preexisting relationships with sanctioned persons or jurisdictions. This is particularly relevant for target companies that have preexisting relationships with Iran and Cuba, given that under these sanctions programs non-U.S. entities owned or controlled by U.S. persons are themselves required to adhere to Iran and Cuba sanctions.¹⁴

Consistent with other recent sanctions enforcement actions,¹⁵ this case also highlights the importance of performing heightened due diligence with regard to potential acquisition targets, joint venture partners, customers, and other counterparties known to engage in business with sanctioned jurisdictions or persons or that otherwise pose elevated risk profiles due to their geographic location, customers, suppliers, or products. This is also consistent with FinCEN's 2018 advisory on Iran's attempts to exploit the U.S. financial system, which recommends enhanced due diligence for transactions originating from or otherwise involving jurisdictions in close proximity to Iran.¹⁶

Finally, this case also demonstrates that robust pre-acquisition sanctions due diligence and post-acquisition sanctions compliance enhancements (including the availability of an ethics hotline for the reporting of potential misconduct to U.S. headquarters) can serve as important mitigating factors in the OFAC enforcement context. Despite the strong aggravating factors present in this case, all of which are factors OFAC considers in determining whether conduct is egregious (willful violations of OFAC sanctions and concealment of those violations, management awareness of conduct leading to the apparent violations, and harm to U.S. sanctions objectives), OFAC nevertheless determined that the conduct at issue was non-egregious. This resulted in a base penalty of \$7,343, whereas the base penalty would have been \$750,000 if OFAC determined the case to be egregious. This demonstrates that although OFAC determined it was appropriate to proceed with a civil penalty, Kollmorgen's "extensive preventative and remedial conduct" had a significant impact on the size of the penalty imposed.

We will continue to monitor sanctions developments and look forward to providing you with further updates.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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¹ U.S. Dep't of Treasury, OFAC, *Kollmorgen Corporation Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations* (Feb. 7, 2019), available [here](#) ("OFAC Web Notice").

² *Id.*

³ *Id.*

⁴ *Id.* At 1-2.

⁵ See 31 C.F.R. part 560.

⁶ OFAC Web Notice at 2.

⁷ *Id.*

⁸ *Id.*

⁹ See 31 C.F.R. part 501, app. A. "General Factors Affecting Administrative Action."

¹⁰ OFAC Web Notice at 3.

¹¹ *Id.*

¹² *Id.*

¹³ U.S. Dep't of Treasury, OFAC, *Treasury Sanctions Turkish National as Foreign Sanctions Evader due to Repeated Violations of U.S. Sanctions Against Iran*, available [here](#) (emphasis added).

¹⁴ See Cuban Assets Control Regulations, 31 C.F.R. 515.329.

¹⁵ For example, the OFAC Epsilon Electronics, Inc. settlement demonstrates that the UAE remains a higher-risk jurisdiction for Iran-related transactions (U.S. Dep't of the Treasury, OFAC, *Epsilon Electronics, Inc. Settles Potential Civil Liability for Alleged*

Violations of the Iranian Transactions and Sanctions Regulations and Related Claims (Sept. 13, 2018), available [here](#)); and the OFAC resolutions with Jereh Oil Field Services Group Co., Ltd (U.S. Dep't of the Treasury, OFAC, *Yantai Jereh Oilfield Services Group Co., Ltd. Settles Potential Civil Liability for Apparent Violations of the Iranian Transactions and Sanctions Regulations* (Dec. 12, 2018), available [here](#)) and e.l.f. Cosmetics, Inc. (See Paul, Weiss, *OFAC Reaches Settlement with e.l.f. Cosmetics, Inc. for North Korea Sanctions Violations Resulting from Inadequate Supply Chain Due Diligence* (Feb. 4, 2019), available [here](#)) involved transactions with China.

¹⁶ U.S. Dep't of the Treasury, Fin. Crimes Enforcement Network, *Advisory on the Iranian Regime's Illicit and Malign Activities and Attempts to Exploit the Financial System*, FIN-2018-Ao06 (Oct. 11, 2018), available [here](#).