

December 9, 2019

## **OFAC Enforcement Action against U.S. Aviation Company Shows the Importance of Ongoing Monitoring over the Course of a Contractual Relationship**

### **Sanctions Contractual Provisions Were Insufficient to Avoid OFAC Liability**

On November 7, 2019, the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC") announced a \$210,600 settlement agreement with Florida-based Apollo Aviation Group, LLC ("Apollo Aviation") to resolve 12 apparent violations of OFAC's Sudan Sanctions Regulations ("SSR").<sup>1</sup> OFAC determined that Apollo Aviation had leased three aircraft engines to a UAE company that subleased the engines to an airline in Ukraine that, in turn, installed the engines on an aircraft that was wet leased to Sudan Airways, which was an entity blocked by OFAC at the time.<sup>2</sup> Under U.S. law, U.S. companies can be held liable for the subleasing or other temporary transfers of items they own to sanctioned countries or persons.

Although Apollo Aviation's lease agreements with the UAE company included U.S. sanctions commitments, OFAC faulted Apollo Aviation for failing to take steps during the terms of the leases to monitor whether the aircraft engines were being used in a sanctions-compliant manner. OFAC noted in particular that Apollo Aviation did not require U.S. export compliance certificates from its lessees and sublessees; beyond this, OFAC did not specify what other monitoring measures the company should have adopted. In announcing the settlement, OFAC observed that aviation is a high-risk industry with respect to U.S. sanctions and referred to its recent advisory (in the Iran context) noting deceptive practices in the aviation industry. OFAC stated that the action highlights, among other things, "the importance of companies operating internationally to implement Know Your Customer screening procedures and implement compliance measures that extend beyond the point-of-sale and function throughout the entire business or lease period."<sup>3</sup>

OFAC's action is a reminder that sanctions contractual clauses, while important, will not shield a company from liability when a counterparty permits sanctioned jurisdictions or persons to use products owned by the company. Depending on the circumstances and the level of sanctions risk involved (which is determined by the industry, counterparties, geographies, and other factors), companies may need to take additional measures after the point of initial transfer to monitor whether their counterparties are complying with U.S. sanctions restrictions.

Below, we provide more detail on OFAC's enforcement action and its implications.

---

### **The Apparent Violations**

According to OFAC, Apollo Aviation entered into agreements with an unnamed UAE company for the lease of two aircraft engines and eventually leased a third aircraft engine to the same UAE company. These engines ultimately ended up being installed on aircraft that were wet leased<sup>4</sup> to an entity blocked by OFAC, Sudan Airways, and that were used for air travel to or in Sudan. The lease agreements into which Apollo Aviation entered with the unnamed UAE company included a sanctions-related provision prohibiting the lessee from maintaining, operating, flying, or transferring the engines to or on behalf of any countries that were the target of comprehensive U.S. sanctions.<sup>5</sup> However, OFAC specifically noted that Apollo Aviation did not obtain U.S. export law compliance certificates from the lessee or sublessees.

According to OFAC, in July 2013, Apollo Aviation leased two aircraft engines to the UAE company, which in turn subleased them to the Ukrainian airline that ultimately installed them on an aircraft that was wet leased to Sudan Airways. Sudan Airways used these two engines for approximately four months, from November 2014 to February 2015. The lease ended in March 2015 and the two engines were returned to Apollo Aviation at that time. In May 2015, Apollo Aviation leased a third aircraft engine to the UAE company, which also was installed on an aircraft that was wet leased to Sudan Airways. Sudan Airways used this engine for approximately four months from May 2015 to September 2015, when it was removed at the request of Apollo Aviation.

When the two engines were returned to Apollo Aviation, they were accompanied by detailed engine records, which included specific information regarding their use and destinations. According to OFAC, a post-lease review of these engine records was not performed by Apollo Aviation until several months later, in August 2015. This review led to Apollo Aviation's discovery that the engines had been used in Sudan by Sudan Airways. Apollo Aviation then contacted the UAE company and discovered that the third engine was currently on an aircraft that had been leased to Sudan Airways. Apollo Aviation then demanded that the UAE company remove this engine from the aircraft, which was completed in September 2015.

OFAC determined that Apollo Aviation appeared to have violated Sections 538.201 and 538.205 of the SSR when its leased engines were installed on an aircraft leased to Sudan Airways, which was a blocked entity at the time (because it met the definition of "Government of Sudan" in the SSR).<sup>6</sup> At the time of the apparent violations, Section 538.201 prohibited U.S. persons from dealing in any property or interests in property of the Government of Sudan and Section 538.205 prohibited the exportation or re-exportation, directly or indirectly, of any goods, technology, or services from the United States or by U.S. persons to Sudan.<sup>7</sup>

OFAC stated that, despite the sanctions-related provisions that Apollo Aviation had included in the lease agreement, Apollo Aviation "did not ensure the aircraft engines were utilized in a manner that complied with OFAC's regulations."<sup>8</sup> OFAC noted that, in addition to not obtaining U.S. export compliance certificates, Apollo Aviation did not periodically monitor or otherwise verify its lessee's adherence to the provisions regarding compliance with U.S. sanctions during the life of the lease. Although not specifically stated by OFAC, if Apollo Aviation had obtained an accurate export compliance certificate from each lessee

and sublessee, it would have been able to identify Sudan Airways' involvement prior to the installation of the engines on the wet leased aircraft, which had occurred two years before Apollo Aviation's review of the engine records identified the apparent violations.

According to OFAC, as a result of this failure to monitor its lessee's adherence to the lease agreement's sanctions provisions, Apollo Aviation did not learn where its engines had actually flown until after the engines were returned to Apollo Aviation at the end of the first lease. OFAC also noted that Apollo Aviation is a large and sophisticated investment manager in the aviation industry, which OFAC described as a high-risk industry from a U.S. sanctions compliance perspective. OFAC pointed to its July 2019 advisory to the civil aviation industry regarding Iran's deceptive practices with respect to aviation products and services and noted that "participants in the civil aviation industry should be aware that other jurisdictions subject to OFAC sanctions may engage in similar deceptive practices."<sup>9</sup>

### **Factors Affecting OFAC's Penalty Determination**

OFAC indicated that Apollo Aviation 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 \$3,000,000, and the base penalty amount was \$360,000.

OFAC noted as aggravating factors that Apollo Aviation is a large and sophisticated entity and that, although the unnamed UAE company appears to have violated the terms of its engine leases prohibiting any use of the engines in sanctioned countries, "Apollo [Aviation] failed to monitor or otherwise verify the actual whereabouts of these aircraft engines during the life of its leases."<sup>10</sup>

Among the mitigating factors OFAC noted was that no Apollo Aviation personnel had "actual knowledge of the conduct leading to the apparent violations," and that the company had implemented a number of remedial measures, which included the following:

- "Apollo [Aviation] improved its Know-Your-Customer screening procedures in keeping with global best practices;"
- "Apollo [Aviation] enhanced employee training on U.S. export law, including by making employees aware of the screening process used by the company; and"
- "Apollo [Aviation] began obtaining U.S. law export compliance certificates from lessees and sublessees."<sup>11</sup>

### **Implications**

The Apollo Aviation settlement agreement shows the importance of not only including contractual provisions regarding sanctions compliance, but also—depending on the circumstances and the level of risk involved—having procedures in place to monitor and verify contractual counterparties' compliance with

---

those provisions during the life of a business relationship. As made clear in its Framework for OFAC Compliance Commitments,<sup>12</sup> OFAC expects companies to take a risk-based approach to sanctions compliance and to implement compliance measures that address the sanctions compliance risks of its operations. In the Apollo Aviation settlement, OFAC noted that the aviation industry is high-risk from a sanctions compliance perspective and that OFAC had issued an advisory (in the Iran context) on deceptive practices in the aviation industry.

Consistent with other recent sanctions enforcement actions,<sup>13</sup> this action also highlights the importance of performing heightened due diligence with regard to potential customers, joint venture partners, acquisition targets and other counterparties with elevated risk profiles due to their geographic location, customers, suppliers, or products. While OFAC did not specifically note this in its announcement of the settlement, the UAE has generally been regarded as a higher-risk jurisdiction from a sanctions compliance perspective. In the Apollo Aviation settlement, OFAC particularly focused on sanctions-related compliance measures that extend beyond the beginning of a business relationship. Although no Apollo Aviation personnel had knowledge of the engines' use in Sudan prior to August 2015, OFAC faulted Apollo Aviation for "fail[ing] to monitor or otherwise verify the actual whereabouts of these aircraft engines during the life of its leases," which had started two years earlier.<sup>14</sup> By contrast, OFAC looked favorably on Apollo Aviation's remedial measures (noted above).

In light of this action, it is important for companies to consider whether their compliance measures at and following the beginning of a business relationship are commensurate with the relevant risks and in keeping with OFAC's evolving expectations. Even apart from factors such as the industry, counterparty, and geography that bear on risk, there are also a number of factors relating to the types of goods or services at issue and the feasibility of monitoring measures that will bear on what strategies companies may reasonably take to monitor sanctions compliance risk over the course of a contractual relationship. There are no one-size-fits-all solutions, but OFAC is sending the clear message that sanctions contractual provisions will not, by themselves, be a shield to liability and that OFAC will often expect companies to take additional measures to monitor and minimize sanctions risk.

\* \* \*

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:

H. Christopher Boehning  
+1-212-373-3061  
[cboehning@paulweiss.com](mailto:cboehning@paulweiss.com)

Jessica S. Carey  
+1-212-373-3566  
[jcarey@paulweiss.com](mailto:jcarey@paulweiss.com)

Christopher D. Frey  
+81-3-3597-6309  
[cfrey@paulweiss.com](mailto:cfrey@paulweiss.com)

Michael E. Gertzman  
+1-212-373-3281  
[mgertzman@paulweiss.com](mailto:mgertzman@paulweiss.com)

Roberto J. Gonzalez  
+1-202-223-7316  
[rgonzalez@paulweiss.com](mailto:rgonzalez@paulweiss.com)

Brad S. Karp  
+1-212-373-3316  
[bkarp@paulweiss.com](mailto:bkarp@paulweiss.com)

Richard S. Elliott  
+1-202-223-7324  
[relliott@paulweiss.com](mailto:relliott@paulweiss.com)

Karen R. King  
+1-212-373-3784  
[kking@paulweiss.com](mailto:kking@paulweiss.com)

*Associate Joshua R. Thompson contributed to this client alert.*

---

<sup>1</sup> U.S. Dep't of the Treasury, OFAC, *Apollo Aviation Group, LLC Settles Potential Civil Liability for Apparent Violations of Sudanese Sanctions Regulations* (Nov. 7, 2019), available [here](#) ("OFAC Web Notice").

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> A "wet lease" is an aviation leasing arrangement whereby the lessor operates the aircraft on behalf of the lessee with the lessor typically providing the crew, maintenance, and insurance, as well as the aircraft itself.

<sup>5</sup> OFAC Web Notice at 1-2.

<sup>6</sup> *See* 31 C.F.R. part 538.

<sup>7</sup> Since January 17, 2017, virtually all transactions that had been prohibited under the SSR are authorized pursuant to a general license located at 31 C.F.R. § 538.540.

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> OFAC Web Notice at 3.

<sup>11</sup> *Id.*

<sup>12</sup> *See* Paul, Weiss, *OFAC Issues Guidance on Sanctions Compliance Programs and Flags "Root Causes" Underlying Prior Enforcement Actions* (May 14, 2019), available [here](#).

<sup>13</sup> *See, e.g.*, The OFAC Kollmorgen Corporation settlement demonstrates that U.S. companies can be held liable for post-acquisition violations by their non-U.S. subsidiaries, even if the U.S. company performs extensive pre-acquisition sanctions-

---

related diligence and does not have knowledge of the violations (see Paul, Weiss, *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* (Feb. 11, 2019), available [here](#)); 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.

<sup>14</sup> OFAC Web Notice at 3.