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# U.S. District Court Agrees with Exxon in Challenge to \$2 Million OFAC Penalty

*By Tal Machnes and Michael Roig\**

*The authors discuss a recent federal district court decision—an unlikely victory for a company challenging Office of Foreign Asset Control sanctions—with potential implications for future sanctions-related enforcement.*

In July 2017, the U.S. Department of Treasury, Office of Foreign Assets Control (“OFAC”) imposed a \$2 million civil penalty on Exxon Mobil Corporation for allegedly violating certain U.S. sanctions involving Russia/Ukraine (the “Regulations”), which had been promulgated under the Obama administration.<sup>1</sup> In a rare move, Exxon responded by suing OFAC in federal district court, challenging the penalty.

The U.S. District Court for the Northern District of Texas granted Exxon’s motion for summary judgment in the case, vacating OFAC’s \$2 million fine against the company.<sup>2</sup>

The district court concluded that the OFAC penalty violated the Due Process Clause of the Fifth Amendment by failing to give Exxon fair notice that its conduct ran afoul of the Regulations.<sup>3</sup> In fact, OFAC *had* issued informal guidance making clear that the conduct at issue was precisely the type of conduct that fell within OFAC’s broad sanctions prohibitions on the receipt of services from sanctioned individuals—but that informal guidance had been issued in the context of an entirely different sanctions program, not in the context of the Russia/Ukraine-related sanctions.

OFAC has since issued similar guidance in the context of the Russia/Ukraine-related sanctions, but only after the conduct at issue had taken place.

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<sup>1</sup> U.S. Dep’t of Treasury, OFAC Enf. Info. for July 20, 2017, *available at* [https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20170720\\_exxonmobil.pdf](https://www.treasury.gov/resource-center/sanctions/CivPen/Documents/20170720_exxonmobil.pdf).

<sup>2</sup> *Exxon Mobil Corp. v. Mnuchin*, No. 3:17-CV-1930-B (N.D. Tex. Dec. 31, 2019).

<sup>3</sup> *Id.* Exxon challenged the penalty on three grounds, but the court—finding for Exxon on Due Process—did not reach the merits on the alternative grounds.

Thus, among other potential implications discussed below, the court's decision in *Exxon* may cause OFAC to issue informal guidance more consistently across its various sanctions programs, where relevant, to ensure that there is no confusion as to the scope of any particular piece of guidance.

## BACKGROUND

The 2017 civil penalty against Exxon was based on certain U.S. sanctions laws imposed during the Obama administration, which were aimed at Russia's assertion of governmental authority in the Crimea region of the Ukraine.<sup>4</sup> OFAC claimed that Exxon—by entering into a series of contracts with Rosneft OAO, a Russian oil company—violated a provision of the Russia/Ukraine-related sanctions which prohibits U.S. companies (and others subject to U.S. jurisdiction) from receiving services from individuals or entities identified on OFAC's list of Specially Designated Nationals and Blocked Persons (“SDNs” or the “SDN List”).<sup>5</sup>

At the time Exxon had entered into those contracts, Rosneft was not on the SDN List. However, an individual named Igor Sechin—Rosneft's president and the chairperson of its management board who had signed the contracts on behalf of Rosneft—*was* on the SDN List, pursuant to EO 13661.<sup>6</sup>

In its motion for summary judgment, Exxon argued that it was not dealing with Sechin in his personal capacity in signing the applicable contracts with Rosneft; rather, Exxon was only dealing with Sechin as an official representative of Rosneft. In other words, Exxon asserted that it had “‘transacted’ solely with *Rosneft*[:]; it dealt only with Rosneft's property [and] services[:; and] the property or services of a designated person such as Sechin are not blocked unless and until the property or services are in the United States or come ‘within the possession or control of any United States person’ ” (which was not the case when Exxon merely signed a contract with Rosneft).<sup>7</sup>

Therefore, Exxon argued, Mr. Sechin's SDN designation was irrelevant, and nothing in OFAC's regulations or guidance on the Russia/Ukraine-related sanctions, specifically, suggested otherwise.

Unsurprisingly, OFAC rejected this and Exxon's other arguments, taking the position that there is no distinction between Mr. Sechin (or any SDN) acting

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<sup>4</sup> *Id.*; see generally 31 C.F.R. Part 589 *et seq.*

<sup>5</sup> OFAC Enf. Info. for July 20, 2017; Exec. Order 13661 of March 16, 2014 (“EO 13661”), Blocking Property of Additional Persons Contributing to the Situation in Ukraine, 79 Fed. Reg. 15,535.

<sup>6</sup> *Exxon*, *supra* n. 2.

<sup>7</sup> See, e.g., Exxon Motion for Summary Judgment, No. 3:17-CV-1930-B, Docket Entry 93 (Aug. 26, 2019).

in a personal versus official capacity.<sup>8</sup> OFAC argued that a designated individual or entity is always a designated individual or entity, regardless of the capacity in which that individual or entity acts, and that U.S. individuals and companies, such as Exxon, are prohibited from dealing with such designated persons, in the broadest sense of that term.

### **EXXON'S SUMMARY JUDGMENT VICTORY**

In granting Exxon's motion for summary judgment, the Northern District of Texas engaged in the rare exercise of resolving an asserted ambiguity in OFAC's sanctions regulations.

Ultimately, the court agreed with Exxon that the Regulations did not provide fair notice that Sechin's role of merely signing contracts on behalf of a non-SDN company would constitute a prohibited "service" under the Regulations. The court reached its conclusion by analyzing the text of the regulations themselves, as well as various statements and guidance issued by the U.S. government surrounding those regulations.

The court's decision may have several important implications for OFAC enforcement more generally.

### **PROHIBITED "SERVICES"**

The \$2 million fine against Exxon in 2017 was based on OFAC's position that Exxon had received prohibited services from Sechin, an SDN, when Sechin signed the contracts at issue on behalf of Rosneft, a non-SDN. The court's decision vacating the fine against Exxon provides an important analysis of the sometimes-amorphous application of the term "services" in the context of U.S. sanctions regulations. OFAC's position on this issue was that a "common meaning of service" in the context of U.S. sanctions regulations "includes providing a 'benefit' to a person, and Mr. Sechin plainly provided a benefit to [Exxon]. . . ."<sup>9</sup>

Indeed, although the court acknowledged that EO 13661 broadly prohibits "services of any nature whatsoever," "suggesting a broad interpretation of services throughout the Regulations," the court ultimately found that the

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<sup>8</sup> See, e.g., *id.*, Appendix in Support of OFAC's Opposition and Cross Motion for Summary Judgment, Docket Entry 98 (Sept. 16, 2019); see also OFAC Press Release, Enforcement Action for July 20, 2017, ("[T]he plain language of [the sanctions does] not contain a 'personal' versus 'professional' distinction, and OFAC has neither interpreted its Regulations in that manner nor endorsed such a distinction.").

<sup>9</sup> *Exxon*, *supra* n. 2.



“regulations are silent” as to what, precisely, constitutes receipt of services.<sup>10</sup> Specifically, on this issue, the court explained:

Regardless of the breadth of the Government’s interpretation, the Court finds that the text of the Regulations does not provide fair notice of its interpretation. First, the text fails to address what constitutes a ‘receipt’ of services. Do the Regulations prohibit any incidental receipt of a benefit resulting from the services? If so, Exxon’s conduct violates the Regulations—after all, Rosneft was contractually bound to fulfill its obligations to Exxon only after Sechin signed the documents. Or do the Regulations limit “receipt” to circumstances in which an SDN’s services are aimed at benefitting a U.S. person? In that case, Exxon would violate the Regulations where Sechin signed on Exxon’s behalf—not where Sechin signed on Rosneft’s behalf. The distinction is subtle, but it is nonetheless meaningful.<sup>11</sup>

Ultimately, the court concluded that the text of the Russia/Ukraine-related sanctions Regulations themselves, on their face, do not resolve these questions, and thus, did not “‘fairly address’ whether a U.S. entity receives a service from an SDN when that SDN performs a service enabling the U.S. person to contract with a non-blocked entity.”<sup>12</sup>

### **ALL FAQs ARE NOT EQUAL: OTHER “FAIR NOTICE” FACTORS**

The court also rejected OFAC’s argument that any claimed ambiguity as to the scope of prohibited services in the Regulations had been clarified by informal guidance issued by OFAC, at the time Exxon entered into the contracts at issue.

The most significant of such guidance was issued by OFAC in 2013, prior to the conduct at issue in the *Exxon* case. “FAQ 285” was a publicly available statement issued by OFAC in the context of its Burma-related sanctions regulations. In relevant part, FAQ 285 stated that “U.S. persons should . . . be

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<sup>10</sup> *Id.* (“But the Court must still determine whether the text of the Regulations provides fair notice that Exxon’s transactions violate Section 4 by constituting the *receipt* of Sechin’s services. . . . Put differently, did Exxon have fair notice, based on the language of the Regulations, that Sechin’s signing of the contracts was a service received by Exxon?”) (emphasis in original).

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

<sup>12</sup> *Id.* The alleged ambiguity with respect to the prohibited receipt of services was critical in Exxon’s case, although we note that the same argument would be unlikely to prevail again today because, as discussed below, OFAC has since issued informal guidance to clarify its position on the issue.

cautious in dealings with [a non-designated entity] to ensure that they are not, for example, entering into any contracts that are signed by the SDN.”<sup>13</sup>

However, it was not until August 2014—*after* Exxon had executed the contracts at issue with Rosneft—that OFAC issued an FAQ in the Russia/Ukraine-related context that mirrored FAQ 285. Nonetheless, the government argued that the Burma-related guidance, available publicly on OFAC’s own website, should have given Exxon fair notice that their business with Rosneft—conducted through an SDN—would have fallen within the scope of OFAC’s prohibitions on dealings with SDNs generally, including those designated pursuant to its Russia/Ukraine-related sanctions.

The court disagreed with OFAC, for several reasons, dismissing the asserted import of the Burma-specific FAQ 285, and finding that OFAC’s after-the-fact guidance in the Russia/Ukraine-related sanctions context actually supported the conclusion that those Regulations had been unclear and failed to provide fair notice at the time Exxon signed the contracts at issue.<sup>14</sup>

First, the court concluded that OFAC’s informal guidance in the context of one sanctions regime *does not* constitute guidance for the purposes of another sanctions regime. Indeed, in an FAQ issued as early as 2006, OFAC itself warned that “[b]ecause each [sanctions] program is based on different foreign policy and national security goals, prohibitions may vary between programs.”

Similarly, in the specific context of the Russia/Ukraine-related sanctions, OFAC made a similar statement—i.e., that “[d]iffering foreign policy and national security circumstances may result in differing interpretations of similar language among the parts of this chapter.”<sup>15</sup> For the court in *Exxon*, these OFAC disclaimers negated any notice FAQ 285 may have otherwise provided.<sup>16</sup> This finding is particularly relevant in the context of OFAC’s sprawling set of sanctions regulations. Often, when faced with a thorny sanctions-related question, companies and practitioners scour OFAC’s FAQs both within and outside the applicable sanctions regime to get some insight into OFAC’s likely position. In *Exxon*, the court has called into question whether OFAC can or should expect this practice going forward.

Second, alongside the relevant FAQs, the court relied on policy statements that U.S. officials had made when promulgating the relevant sanctions involving Crimea.

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<sup>13</sup> See OFAC Enf. Info. for July 20, 2017. OFAC has since issued similar guidance in the context of other U.S. sanctions programs, as well.

<sup>14</sup> *Id.* at \*9.

<sup>15</sup> 31 C.F.R. § 589.101.

<sup>16</sup> *Exxon*, *supra* n. 2.

For instance, the day after the issuance of EO 13661, the White House released a “Fact Sheet” on the new Russia/Ukraine-related sanctions, which stated: “Our current focus is to identify [certain] individuals [contributing to the situation in Crimea] and target their personal assets, but not companies that they may manage on behalf of the Russian state.”<sup>17</sup> The court in *Exxon* noted that this statement—in addition to several other Executive branch statements—would “likely lead a regulated party, acting in good faith, to hesitate before completing transactions like Exxon’s, [but] they do not create ascertainable certainty that such conduct would be prohibited.”<sup>18</sup>

Finally, while the government argued that Exxon could have sought guidance from OFAC to the extent it viewed these statements as ambiguous or conflicting, the court disagreed.<sup>19</sup> The court determined that Exxon’s failure to inquire as to the meaning of the regulations was relevant to its decision, but not dispositive. With respect to this factor, the court emphasized that the burden of creating fair notice rests on the regulators, not the regulated.

## IMPLICATIONS FOR OFAC ADMINISTRATIVE RECORDS

The court’s consideration of one additional factor in *Exxon* bears noting. Specifically, the court dismissed Exxon’s argument that OFAC’s “internal uncertainty” as to the correct interpretation of the regulations prevented the company from having fair notice as to the meaning of the regulations.<sup>20</sup>

While there is case law to support the proposition that open *disagreement* within an agency may affect the question of notice, internal uncertainty or deliberation does not. After months of litigation between the parties in which Exxon pushed for OFAC to release more unredacted portions of the agency’s administrative record substantiating its penalty against Exxon, which the court ultimately ordered OFAC to do, this was an important ruling that protected the agency’s internal deliberations.

## CONCLUSION

Although this decision may be viewed by many as a weak spot in OFAC’s armor, there is reason for caution. Exxon’s victory, of course, is limited to the Texas courtroom, and OFAC may appeal the decision. More importantly, OFAC may view the decision as limiting its ability to bring novel enforcement

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<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

<sup>20</sup> *Id.*

actions, but is unlikely to be deterred in enforcing the myriad prohibitions under its sanctions programs for which there is already thorough guidance and documentation.

Indeed, the *Exxon* decision may lead OFAC to issue more consistent informal guidance across its various sanctions programs, where relevant, to ensure that there is no confusion as to the scope of any one particular FAQ.

Moreover, despite Exxon's decision to challenge OFAC's 2017 penalty, the company ultimately decided to stop pursuing its venture with Rosneft, at least in part as a result of other U.S. sanctions-related considerations, anyway.<sup>21</sup> This underscores the fact that, even where companies are willing to be aggressive in countering OFAC's actions, those same companies continue to be cautious and take seriously the importance of sanctions compliance.

More generally, after a year of record-high enforcement by OFAC against companies across many different sanctions programs, whether Exxon's unlikely win portends less aggressive OFAC enforcement for 2020 remains to be seen.

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<sup>21</sup> See, e.g., R. Gold, *U.S. Sanctions, Low Oil Prices Doomed Exxon's Russian Projects*, Wall Street J., Mar. 1, 2018), available at <https://www.wsj.com/articles/exxon-abandons-russian-projects-brokered-by-tillerson-1519897033>.