

Corporate Counsel

Sanctions

Al Haramain: Analyzing the Impact of the Ninth Circuit's Recent Decision on OFAC's Jurisdiction

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Introduction

The Department of Treasury's Office of Foreign Assets Control (OFAC) is responsible for administering and enforcing economic sanctions and embargoes designed to advance the United States' foreign policy and national security interests. Over the last few years, OFAC has not only increased its enforcement activities significantly, it has also—due principally to new federal legislation enacted in October 2007—increased the amount of penalties it has recovered. Between 2007 and 2009, the amount of civil penalties and settlements OFAC collected jumped from \$3.5M to approximately \$1B. Criminal enforcement actions have risen during that time frame as well.

The upshot of the increased enforcement and enhanced penalties is that individuals and companies subject to the OFAC's jurisdiction are exposed to more severe civil penalties and criminal liability than ever before. Because so few OFAC cases ever reach final adjudication before a fact finder, any decision analyzing OFAC issues is all the more important. A recent decision by the U.S. Court of Appeals for the Ninth Circuit, *Al Haramain Islamic Foundation v. United States Dep't of Treasury*,¹ could have significant OFAC implications for U.S. companies,

multinational corporations, and U.S. citizens. More specifically, the court's interpretation of the phrase "owned or controlled by" may expand the scope of potential liability for a wide range of U.S. citizens as well as entities organized in the United States and abroad.

The *Al Haramain* Decision

— A. Background

Shortly after the events of September 11, 2001, President Bush blocked the assets of 27 persons through Executive Order 13224.² President Bush also delegated authority to the Secretary of Treasury "to designate other foreign groups or individuals who have committed or who pose a risk of committing acts of terrorism, or who are owned or controlled by, or . . . act for or on behalf of those entities designated by the President or those subsequently designated by the Secretary of Treasury." *Al Haramain Islamic Found., Inc. v. United States Dep't of Treasury* (internal quotations omitted).³

Pursuant to this Executive Order, OFAC blocked the assets of the Al Haramain Islamic Foundation (AHIF-Oregon)—a non-profit organization domiciled in Oregon—pending an investigation in February 2004.⁴ AHIF-Oregon was one of many organizations across the world using the Al Haramain Islamic Foundation name, including the Al Haramain Islamic Foundation in Saudi Arabia (AHIF-Saudi Arabia).⁵ Consistent with its general practice, OFAC did not provide AHIF-Oregon prior notice or obtain a warrant before blocking its assets.⁶ Shortly after freezing AHIF-Oregon's assets, OFAC published a press release that explained it had blocked AHIF-Oregon's assets because its "parent" was located in Saudi Arabia and OFAC had blocked the assets of AHIF branches in other countries.⁷ In April 2004, OFAC provided AHIF-Oregon unclassified documents, "asserting that it was considering designating AHIF-Oregon as a [specially designated global terrorist

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(SDGT)] on the basis of [the information in the press release] as well as classified documents it did not disclose.”⁸ In the following months, OFAC sent AHIF-Oregon a “supplemental record” as well as additional unclassified documents.⁹ In September 2004, OFAC issued another press release stating that it had designated AHIF-Oregon as a SDGT.¹⁰ The press release also stated that OFAC had designated Soliman Al-Buthe, a Saudi national that founded AHIF-Oregon, served on its Board of Directors, and was prominently involved with AHIF-Saudi Arabia.¹¹ Neither AHIF-Oregon nor Al-Buthe received a comprehensive explanation for why OFAC had designated them as SDGTs.¹²

Following its designation, AHIF-Oregon filed a request for administrative reconsideration in early 2005, but never received a response.¹³ In February 2008, OFAC sent AHIF-Oregon a letter explaining that it was redesignating the organization as a SDGT because it was: (1) being owned or controlled by Al-Buthe; (2) acting for or on behalf of Al-Buthe; and (3) supporting and operating as a branch office of AHIF-Saudi Arabia and in that capacity “had acted for or on behalf of, or has assisted in, sponsored, or provided financial, material, or technological support, or financial or other services to or in support of Al Qaida and other SDGTs.”¹⁴ AHIF-Oregon filed suit in federal district court challenging OFAC’s actions on several grounds.¹⁵ AHIF-Oregon claimed that OFAC’s designation was improper because it was not supported by substantial evidence that (1) AHIF-Oregon was owned or controlled by a designated person or (2) AHIF-Oregon supported terrorism. The district court rejected the first argument, concluding that there was “substantial evidence of Al-Buthe’s ownership or control over AHIF-Oregon at the time of the designation and redesignation.”¹⁶ The district court reasoned that Al-Buthe had ownership or control of AHIF-Oregon because he was listed as the organization’s Treasurer, held a seat on the Board of Directors, signed contracts for AHIF-Oregon, and “was one of only two individuals with access to its bank account.”¹⁷ The district court also found substantial evidence existed “in the classified and unclassified record demonstrating that AHIF-Oregon supported [terrorism] as a branch of [AHIF-Saudi Arabia].”¹⁸

In addition, AHIF-Oregon claimed that OFAC violated its procedural due process and Fourth Amendment rights under the U.S. Constitution. The district court found that OFAC violated AHIF-Oregon’s due process rights by “delaying its notice to AHIF-Oregon about the reasons for contemplating a designation action” in 2004, but determined the violation was harmless.¹⁹ Finally, the district court found that OFAC’s blocking order constituted a seizure within the meaning of the Fourth Amendment, but did not violate AHIF-Oregon’s constitutional rights because it was supported by the “special needs” exception.²⁰ Based on these findings, the district court granted summary judgment to OFAC on all of AHIF-Oregon’s claims.²¹ AHIF-Oregon subsequently appealed, challenging several aspects of the district court’s opinion.

– B. Substantive Challenge to the Redesignation of AHIF-Oregon As A Specially Designated Global Terrorist

On appeal, AHIF-Oregon again argued that there was not substantial evidence to support OFAC’s 2008 redesignation.²² The Ninth Circuit rejected this argument, reasoning that Al-Buthe is a designated party that “exercises control over AHIF-Oregon because he is on the board of directors.”²³ In other words, AHIF-Oregon is owned or controlled by a designated person.²⁴ Because Executive Order 13224 authorized OFAC to designate entities controlled by a designated person as an SDGT, the Ninth Circuit concluded OFAC had “a valid reason to designate AHIF-Oregon based on Al-Buthe’s control.”²⁵

The Ninth Circuit’s reading of the “owned or controlled by” language in Executive Order 13224 could have significant consequences given the ubiquity of the “owned or controlled by” language in the OFAC sanctions regulations. Many sanctions regulations require U.S. persons to block the property of entities that are owned or controlled by designated parties.²⁶ For example, the Sudanese Sanctions Regulations require any property of the “Government of Sudan” that comes into the possession of a United States person to be blocked.²⁷ The “Government of Sudan” is defined as the “state and the Government of Sudan” as well as “[a]ny entity owned or controlled by the” Government of Sudan.²⁸ Additionally, the “owned or controlled by” language expands the scope of OFAC’s jurisdiction in certain sanctions regulations. For example, the Cuban Assets Control Regulations apply to “person[s] subject to the jurisdiction of the United States,” including any citizen or resident of the United States, any entity organized under the laws of the United States, or any entity—wherever located—owned or controlled by such persons.²⁹

The Ninth Circuit’s conclusion that AHIF was controlled by a board member is broader than how the “owned and controlled by” phrase has been historically understood. The earliest relevant guidance regarding the interpretation of “owned or controlled by” was set forth in a 1964 law review article written by Stanley Sommerfield, OFAC’s Chief Counsel at the time.³⁰ In the article, Sommerfield explained that “Treasury has interpreted the term [control] to include any type of effective control, actual or potential.”³¹ In more concrete terms, Sommerfield explained that a person could control an entity by owning fifty percent of the entity’s common stock.³² Additionally, control could also be established if a person owned a smaller percentage of stock provided that the holding was sufficient to provide the stockholder “working control” of the entity.³³

In February 2008, OFAC issued formal guidance that defined ownership and control in an even more restrictive manner.³⁴ In the guidance, OFAC explained that “[a] person whose property and interests in property are blocked pursuant to an Executive order or regulations administered by OFAC . . . is considered to have an interest in all property and interests in property of an entity in which it owns, directly or indirectly, a 50 percent or greater interest.”³⁵ This guidance suggests that a person that had a majority stake in an entity owned or controlled the entity for OFAC purposes, and left open the possibility that a person could

own or control an entity in other ways as well. However, under this guidance, merely holding a board position would not have been sufficient to constitute ownership or control over the entity (absent other factors).

Al Haramain significantly expands the meaning of “owned or controlled by.” While previous guidance suggested that it might be possible for a person with less than a fifty percent stake in an entity to control it, the Ninth Circuit definitively concluded that board membership alone is sufficient to constitute ownership or control. It is unclear on what basis the Ninth Circuit reached this conclusion—the court did not cite to any OFAC cases, agency guidance, or even principles of corporate law to support its conclusion. As a practical matter, it is also unclear how, in the absence of other ownership interests, a board member could have control over a company in any meaningful sense. *Al Haramain* also creates the possibility that an individual could control an entity for OFAC purposes by other means, such as owning a small percentage of its stock (e.g., 10 percent) or holding a senior management position within the company.

To the extent that *Al Haramain* represents the definitive construction of the phrase “owned or controlled by,” it could have two significant effects. First, and most importantly, the decision potentially expands the number and types of entities subject to OFAC’s jurisdiction. For example, imagine a U.S. citizen who sits on the board of a Spanish company that engages in business with Cuban entities. Prior to *Al Haramain*, the participation of a U.S. person on the board of a foreign country that does business with sanctioned parties or embargoed countries would have likely been permissible under U.S. law in the absence of other factors. But under the Ninth Circuit’s analysis, the presence of the U.S. citizen on the board of the Spanish company could mean that a U.S. person controls the entity. Consequently, the Spanish company could be subject to OFAC’s jurisdiction and its business with Cuba could violate the Cuban Assets Control Regulations. This is not a far-fetched hypothetical, but a real problem given that U.S. persons frequently serve on the boards of foreign companies that do business with sanctioned parties and/or embargoed countries.

The other important implication is the reverse scenario: under certain circumstances, U.S. entities could be designated by OFAC on the basis that they are controlled by a sanctioned party if a designated individual sits on the entity’s board. Just as AHIF-Oregon’s property was blocked because Al-Buthe was on their board, other companies’ assets could be frozen on the same basis. To illustrate this issue, assume that a U.S. private equity fund acquired a portfolio company registered and incorporated in Spain that did business with Cuba. In connection with the acquisition, the U.S. private equity company obtained a board seat on the portfolio company that it filled with a U.S. citizen. As discussed above, the portfolio company could be subject to OFAC’s jurisdiction because a U.S. person controls the company. If a designated foreign national also held a board seat on the portfolio company, then the portfolio company (and the board member) might violate the OFAC sanctions regulations because the company could be seen as being controlled by a designated

individual. OFAC could then block the assets of the portfolio company. Additionally, the portfolio company—and possibly even the U.S. person on the board—could face civil and/or criminal liability for violating OFAC sanctions regulations.

If the Ninth Circuit’s reasoning in *Al Haramain* is adopted by other circuits, then it could have a significant effect for U.S. and foreign entities. There are, however, reasons to think the impact of the decision will be limited. On appeal, AHIF-Oregon never argued that Al-Buthe did not exercise control over AHIF-Oregon by serving on its board. Rather, the organization claimed that Al-Buthe’s designation was unfounded “because OFAC gave no reasons for designating Al-Buthe . . . , AHIF-Oregon . . . reasonably assumed that he was designated not for an independent reason germane to him, but because of his connection to AHIF-Oregon.”³⁶ It is possible that the Ninth Circuit would have reached a different outcome if AHIF-Oregon had asserted that Al-Buthe did not control it.

Additionally, Al-Buthe’s presence on AHIF-Oregon’s board was not the only factor that the Ninth Circuit relied on in deciding that substantial evidence supported OFAC’s designation. Based on the classified and unclassified record, the court “conclude[d] confidently that substantial evidence supports OFAC’s conclusion that AHIF-Oregon supported designated persons” in other countries as a branch office of AHIF-Saudi Arabia, which served as an additional justification for OFAC to designate AHIF-Oregon.³⁷ ³⁸ Finally, Ninth Circuit decisions are not always indicative of how other circuits, or the Supreme Court, will resolve an issue. But with that said, *Al Haramain* appears to be the final decision on this issue for now because AHIF-Oregon did not appeal the Ninth Circuit’s decision to the Supreme Court.

– C. Constitutional Issues

In addition to the ownership and control issue, AHIF-Oregon also claimed that OFAC violated its procedural due process and Fourth Amendment rights.

– 1. Procedural Due Process Analysis

AHIF-Oregon argued that OFAC violated its procedural due process rights by relying on classified information to designate AHIF-Oregon, but not disclosing the classified material.³⁹ While the Ninth Circuit held that the use of classified information was not impermissible, it determined that OFAC was required to either provide AHIF-Oregon with an “unclassified summary” of the classified evidence or make the classified material available to a lawyer for AHIF-Oregon with the requisite security clearance.⁴⁰ These measures were necessary, the Ninth Circuit reasoned, because they were not unduly burdensome for OFAC and the sanctions at issue were severe.⁴¹ AHIF-Oregon also made the related argument that OFAC violated its due process rights by not providing it with adequate notice and a meaningful opportunity to respond to the designation.⁴² Approximately seven months after OFAC first designated AHIF-Oregon, it issued a press release

that explained OFAC's reasons for the designation.⁴³ Apart from that release, OFAC did not explain why it had designated AHIF-Oregon during the subsequent four years.⁴⁴ The Ninth Circuit held that OFAC's failure to provide AHIF-Oregon with more detailed information regarding the designation violated its procedural due process rights.⁴⁵ But the court found the violations to be harmless in light of the available evidence because "[e]ven if AHIF-Oregon had enjoyed better access to classified information and constitutionally adequate notice . . . it would not have changed OFAC's ultimate designation determination."⁴⁶

– 2. Fourth Amendment Analysis

The Ninth Circuit also concluded that OFAC's failure to obtain a warrant prior to blocking AHIF-Oregon's assets violated the organization's Fourth Amendment rights.⁴⁷ In reaching this conclusion, the Ninth Circuit found that the blocking of assets constituted a seizure for Fourth Amendment purposes.⁴⁸ The court rejected OFAC's position that the blocking was permissible pursuant to the "special needs" exception to the warrant requirement because it would not be "impracticable for OFAC to achieve its undeniably important aims without securing a warrant."⁴⁹ The Ninth Circuit explained that it would have been permissible for OFAC to initially seize AHIF's assets absent a warrant, but doing so permanently violated the Fourth Amendment.⁵⁰

– 3. Impact of the Court's Due Process and Fourth Amendment Analysis

At first blush, the Ninth Circuit's analysis regarding designated entities procedural due process and Fourth Amendment rights seems to be significant because it appears to open a new avenue for designated parties to challenge OFAC when its property is blocked. In reality, however, very few designated parties will be able to rely on these arguments because only American citizens or U.S. entities have these Constitutional rights. The overwhelming majority of designated parties are foreign nationals. Consequently, the applicability of this part of the *Al Haramain* decision will likely have less of an impact on OFAC policy than the court's holding regarding the scope of ownership and control.

Conclusion

The *Al Haramain* decision raises serious issues that could have significant implications for OFAC enforcement. U.S. and foreign companies should be aware of these issues as courts attempt to clarify this complicated and ambiguous area of law.

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¹ 660 F.3d 1019 (9th Cir. 2011).

² *Id.* at 1023.

³ No. 07-1155-KI, 2009 BL 239968, at *4 (D. Ore. Nov. 5, 2009).

⁴ *Id.* at *5.

⁵ In addition to sharing a name, AHIF-Oregon and AHIF-Saudi Arabia also had common leaders. 2009 BL 239968, at *6 Two Saudi nationals, Aqeel Al-Aqil and Soliman Al-Buthe, were intimately involved in AHIF-Saudi Arabia before founding AHIF-Oregon. *Id.* Al-Aqil helped found AHIF-Oregon and served as the Director of AHIF-Oregon until he was removed in January 2004. *Id.*

⁶ *Id.*

⁷ *Id.* at *6-7.

⁸ *Id.* at *7.

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.* at *8.

¹³ 660 F.3d at 1027.

¹⁴ 2009 BL 239968, at *8.

¹⁵ *Id.* at *2-3.

¹⁶ *Id.* at *8.

¹⁷ *Id.* at *8-9.

¹⁸ *Id.* at *9.

¹⁹ *Id.* at *12.

²⁰ *Id.* at *30.

²¹ 660 F.3d at 1028.

²² *Id.*

²³ *Id.* at 1029.

²⁴ The Ninth Circuit reiterated that AHIF-Oregon was controlled by Al-Buthe several times. 660 F.3d at 1031 ("The evidence in the administrative record demonstrates that Al-Buthe controlled AHIF-Oregon"); see also *id.* ("AHIF-Oregon now has kept on its board of directors a designated person for more than five years, two years since it has known OFAC's reasoning, and that designated person has not challenged OFAC's designation before this court. AHIF-Oregon is 'controlled by' a designated person.").

²⁵ *Id.*

²⁶ See, e.g., Belarus Sanctions Regulations, 31 CFR § 548.201; Syrian Sanctions Regulations, 31 CFR § 542.201.

²⁷ 31 C.F.R. § 538.201 (2009).

²⁸ 31 C.F.R. § 538.305.

²⁹ 31 C.F.R. § 515.329.

³⁰ Stanley L. Sommerfield, *Treasury Regulations Affecting Trade With the Sino-Soviet Bloc and Cuba*, 19 Bus. L. 861 (1964).

³¹ *Id.* at 866.

³² *Id.*

³³ *Id.*

³⁴ See OFAC Guidance on Entities Owned By Persons Whose Property and Interests in Property are Blocked (Feb. 14, 2008).

³⁵ *Id.*

³⁶ 660 F.3d at 1029.

³⁷ The district court concluded that Al-Buthe owned or controlled AHIF-Oregon for several reasons, including that Al-Buthe was listed as Treasurer, had a board seat, signed contracts on AHIF's behalf and was one of two individuals with access to AHIF-Oregon's bank account. The Ninth Circuit did not expressly rely on any of these facts in its analysis, but it is possible that they informed the court's conclusion that Al-Buthe controlled AHIF-Oregon.

³⁸ *Id.* at 1032.

³⁹ *Id.* at 1032.

⁴⁰ *Id.* at 1036-37.

⁴¹ *Id.* at 1037.

⁴² *Id.* at 1038.

⁴³ *Id.* at 1039.

⁴⁴ *Id.*

⁴⁵ *Id.* at 1040.

⁴⁶ *Id.* at 1043.

⁴⁷ *Id.*

⁴⁸ The Ninth's Circuit determination that blocking assets constitutes a seizure was consistent with *KindHearts for Charitable Humanitarian Dev., Inc. v. Geithner*, 647 F. Supp. 2d 857, 878 (N.D. Ohio 2009). Other courts, however, had reached the opposite conclusion. See *Islamic Am. Relief Agency v. Unidentified FBI Agents*, 394 F. Supp. 2d 34, 47-48 (D.D.C. 2005); *Holy Land Foundation for Relief and Development v. Ashcroft*, 219 F. Supp. 2d 57, 79 (D.D.C. 2002).

⁴⁹ *Id.* at 1046.

⁵⁰ *Id.* at 1046-47.