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BNP Paribas – Autopsy of a crime

The penalties against BNP Paribas raised countless issues, be they legal, financial, economic or political. The most frequently asked questions from our clients were the following:

- Are the sanctions imposed on BNP Paribas by US authorities an act of economic war, or are they justified?
- Does this sanction constitute a turning point in US policy that could pose a substantial risk for banks?
- Are banks doomed to "return" all their profits in the form of fines and sanctions?
- Which banks could be next?

Although our analysis will never be as thorough as that of a US lawyer specialising in embargoes, we will try to answer those questions as precisely as possible. Our responses are based on our understanding of (i) US legislation and of (ii) all the documents published by the US Department of Justice (Plea Agreement, Statement of Facts, *etc.*)

First of all, let's have a look at the context.

What are the charges?

In 1997, an Executive Order signed by President Clinton imposed an embargo on Sudan, and it was strengthened by a decision of President Bush in 2006. President Clinton had already taken similar measures regarding Iran in 1995. As for Cuba, the embargo is even older since it dates back from 1960. Thus, BNP Paribas was faced with well-established rules. The legal basis for these presidential decisions lies in two Acts of Congress: the IEEPA (International Emergency Economic Powers Act) which is primarily concerned with terrorism, drug trafficking, etc., and the TWEA (Trading With the Enemy Act), which is currently in place against Cuba and North Korea. This distinction is important since sanctions are considerably lower in the case of the TWEA.

Without going into technicalities, we can simplify the definition of an embargo by considering that these acts prohibit any trade in goods or any transaction denominated in USD with those countries or their state-owned or mixed state- and privately-owned companies. The underlying idea is to isolate them by preventing them from using the world's No.1 currency, that is, the US dollar.
The OFAC, an office of the US Treasury, keeps a list of all sanctions imposed in this context (ten to thirty every year) since 2003. Among the several sanctions previously imposed, we can find payments

from the ATP Tour to Iranian tennis players, as well as medical supplies sales, or bank transfers in USD.

BNP Paribas is basically being charged for allowing Sudan, Iran and Cuba to circumvent the embargo by completing transactions in USD, mainly in the context of the financing of foreign trade. In order to clear USD transactions, BNP Paribas executed them in France or Switzerland and then cleared them with an American bank (part of the BNP group or not) under its own name, without indicating the actual beneficiaries. BNP Paribas acted as a front company for its Sudanese, Iranian or Cuban clients.

Is the amount of penalties fair?

General principle

This is clearly the most important question and we can only offer a partial answer, based on our understanding of the law and the facts as described in settlement agreements.

First, it must be reminded that pursuant to US law, BNP Paribas was facing four potential sanctions:

- A "civil" sanction imposed by the OFAC for violating the embargo;
- A regulatory sanction imposed by the FED;
- A "criminal" sanction for non-compliance with federal laws: conspiring to deliberately get around the embargo is an additional crime compared to the simple fact of getting around the embargo (US Code, Title 50, Section 1705);
- A "criminal" sanction for non-compliance with New York State laws by communicating false information in order to conceal a crime (NY penal law, section 175.10).

Thus, the total penalty paid by BNP Paribas is divided into four components, and the negotiation also focuses on the distribution between these US entities.

After the Congress established higher maximum penalties in 2008, the OFAC published criteria for determining the penalties to be imposed (in 2008 as well). The sanction amount is based on two main criteria: (1) were the violations voluntarily disclosed to the OFAC? and (2) were these violations significant and egregious? The following table presents a summary of the consequences of this classification.

Amount of penalties	Not egregious	Egregious
Violations voluntarily disclosed	50% of the transaction capped at 125k per transaction, and 32.5k for TWEA violations	50% of the highest of the following amounts: 2x the amount of the transaction or 250k, for IEEPA violations 50% of the lowest of the following amounts: amount of the transaction or 65k, for TWEA violations
Violations not voluntarily disclosed	Lowest of the following amounts: scale according to the amount of the transaction, 250k for IEEPA violations, or 65k for TWEA violations	Highest of the following amounts: 2x the amount of the transaction or 250k, for IEEPA violations Lowest of the following amounts: amount of the transaction or 65k, for TWEA violations

As can be seen in this table, the voluntary disclosure of violations has a major impact (by a factor of two) and committing egregious violations basically lifts the cap on the fine. Thus, the total amount of penalties varies considerably whether there are many small violations or a few large violations.

These "base" amounts are later adjusted based on factors such as the cooperation of the companies prosecuted (decrease by 25%-40%) or the absence of prior violations (decrease by 25%).

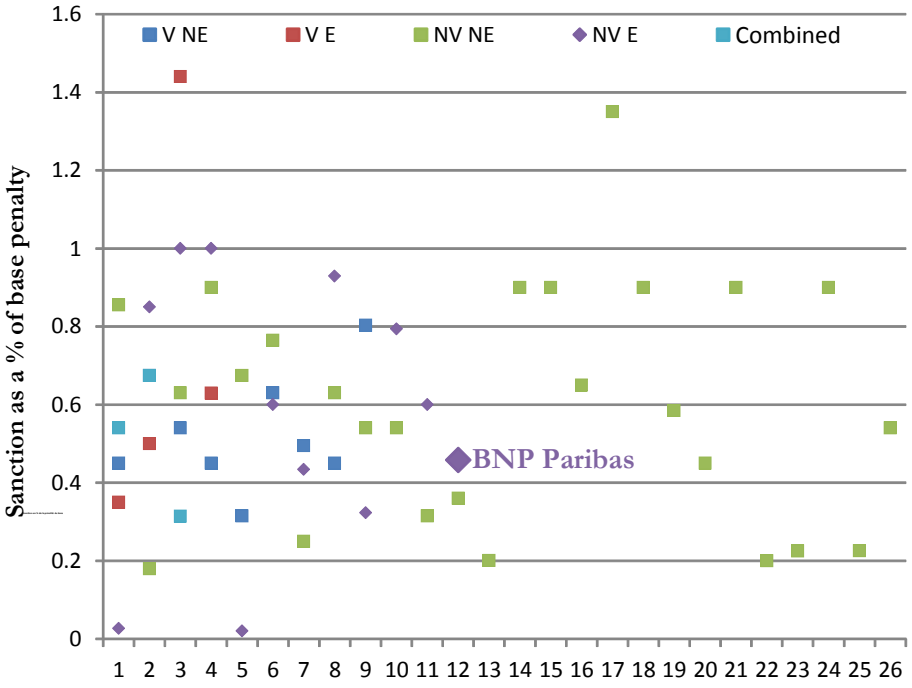
Besides, BNP Paribas was accused of committing criminal offences punishable with imprisonment and with a fine equal to twice the amount of profits obtained from the violations.

Most of the time, when an agreement is reached, including for criminal charges, the resulting financial consequences are attributed to the "civil" sanction imposed by the OFAC.

Case of BNP Paribas

As sanctions have been more transparent since 2012, we compared the one imposed on BNP Paribas to the 53 sanctions imposed since 2012 (which vary from USD9000 to USD619m, excluding BNP Paribas) and to major sanctions imposed on banks since 2009.

The following graph shows the sanction as a percentage of the base penalty calculated based on the criteria described above. The overall average is 59%.



Source: OFAC, Axiom AI.
V: voluntary disclosure; NV: non-voluntary disclosure; E: egregious violation; NE: non-egregious violation

As a percentage of base penalty, the sanction imposed on BNP Paribas seems neither particularly harsh nor particularly lenient. In fact, the only sanctions which stand out are those against Clearstream (USD151m) and Dal-Tech Devices[1] (USD10000) because they were especially lenient and those against American Express and Bank of Guam because they were especially harsh. This graph provides us insight into the figures mentioned in the press: USD20bn is more or less the base penalty that could have been imposed without mitigating factors, and the very optimistic provision of USD1bn entered by BNP Paribas was probably estimated based on the sanction imposed on Clearstream. For instance, ING paid 92% of the base penalty, HSBC 32%, Barclays 80% and Crédit Suisse 31%. BNP Paribas is thus in the middle of the pack.

Now what remains to be assessed is whether the base penalty was fair: according to the facts published by the Department of Justice (and admitted by BNP Paribas, albeit under the threat of a more severe sanction), BNP Paribas did not voluntarily disclose the violations. Considering the facts egregious does not seem an exaggeration since the emails revealed by US authorities seem to indicate that: BNP Paribas deliberately circumvented the embargo; it was using banks as "front companies" without their knowledge in order to conceal the beneficiaries of the operations[2]; several legal opinions were solicited and even if these opinions became very negative from 2006 the bank still ignored them for commercial reasons; the front office was acting with the consent of the management and being fully aware of the risks, as demonstrated by its attempts to change the currency of several operations in order to cover the risk; and credit applications clearly indicated that the complexity of the transactions was only justified in order to get around US embargo rules, etc.

[1] In this case, we do not know the amount of criminal sanctions and they are to be added to the indicated figure.
[2] It was even hiding the truth behind these operations to its own US subsidiary!

Consequently, based on the documents filed with the Justice Department and on purely mechanical rules published in 2008, the result of our calculation of the base penalty (if the facts admitted by BNP Paribas are true) is USD19 109 231 550, whereas the figure obtained by OFAC is USD19 272 380 006. Again, it seems difficult to view this as an unduly harsh punishment.

In conclusion, the BNP case does not seem to mark a turning point in the policy of US authorities, who applied their usual criteria, the same that were applied to ING, HSBC, Barclays, Credit Suisse, and Bank of Tokyo-Mitsubishi UFJ when these banks were sanctioned.

Why did BNP Paribas pay such a huge fine?

The answer lies in several figures:

- USD9 554 615 775.18: the total amount of illegal cash movements admitted by BNP Paribas, much larger than the USD1.7bn admitted by ING, which is the second most-fined bank and which had the good idea to spontaneously disclose some of these operations to US authorities.

- USD160bn: the amount of letters of credit granted by BNP Paribas to embargoed entities. Fortunately, the OFAC did not take this figure into account in its calculation and accepted to consider only physical cash movements (letters of credit often remain undrawn), but the amounts are outrageous.

- 50%: the proportion of Sudan's reserves of foreign exchange held with BNP Paribas Geneva.

- 25%: the proportion of Sudan's foreign trade financed through BNP Paribas Geneva!

There is therefore no mysterious explanation or conspiracy: if the admitted facts are true, BNP Paribas carried out an enormous amount of transactions with Sudan and probably generated very substantial profits from them, in view of which the sanction seems to be proportionate. 87.3% of the sanction corresponds to violations regarding Sudan, 12.36% regarding Iran, 0.31% regarding Cuba and 0.02% regarding Myanmar.

What are the risks for other banks?

As we have just explained, there is no sign of a shift in US policy. The risks faced by banks previously sanctioned seem very low because we tend to believe they will not play with fire again.

Regarding banks that have never been sanctioned, the risk mainly affects dealings with two countries: Sudan and Iran, especially because of their oil exports, which are often financed in USD. A third country, Libya, is to be added to this list even though it is embargoed anymore. ING was mainly sanctioned because of dealings with this country and we fear that Unicredit, whose strategic

shareholders included Libya, carried out illegal transactions with this shareholder since it was a "natural" client, even before the lifting of the embargo.

Moreover, it is quite certain that no other bank –French or other– has such strong relationships with Sudan. In consequence, sanctions as large as that imposed on BNP Paribas do not seem realistic. In contrast, it should be pointed out that, among the major players of foreign trade financing, Deutsche Bank, CASA, Natixis and Unicredit have never been sanctioned and are thus more subject to this risk. We know Société Générale's US subsidiary signed a settlement agreement with the OFAC in 2011 for an amount of USD111k, regarding payment flows of USD330k corresponding to letters of credit guaranteeing the delivery of ships possessed by an Iranian public entity. Société Générale explicitly indicated that it had been subject to an information request and that an audit was in progress, but that potential consequences were not "material". In their 2013 annual reports, Crédit Agricole and Deutsche Bank also mentioned an ongoing cooperation with the OFAC. None of these banks seems to have ever voluntarily disclosed any violation to the OFAC (except Société Générale in 2011).

In any case, we can safely say that one French bank will be sanctioned: in the documents published by the Department of Justice, an email from a BNP Paribas employee states that "*[French Bank 1] knows very well that Cuba or any other Cuban theme must not be mentioned in the transfer orders and I reminded them about this over the phone this morning.*" We do not know who "*French bank 1"* is but US authorities do, and up until now the only French bank sanctioned by the OFAC was Société Générale, regarding operations with Iran. The potential fine regarding these operations will be a lot smaller than that paid by BNP Paribas considering that Cuba only accounts for USD1bn of BNP Paribas's fine and that a "complicit" bank will certainly receive a smaller sanction (for the simple reason that it did not participate in all the operations).