

**IN THE DISTRICT COURT  
AT MANUKAU**

**CRI-2017-092-009166  
CRI-2018-092-002954  
[2018] NZDC 5034**

**NEW ZEALAND CUSTOMS SERVICE**  
Prosecutor

v

**PACIFIC AEROSPACE LIMITED**  
Offender

Hearing: 16 March 2018  
Appearances: Mr J Rhodes for the Prosecutor  
Ms E Rushbrook for the Offender  
Judgment: 29 May 2018

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**RESERVED JUDGMENT OF JUDGE J BERGSENG**  
**[Sentencing]**

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**The Charges**

[1] Pacific Aerospace Limited (PAL) has pleaded guilty to three charges of indirectly exporting a specified good to the Democratic People's Republic of Korea (DPRK)<sup>1</sup> and one charge of making an erroneous export entry.<sup>2</sup> New Zealand Customs Service brings this prosecution (Customs).

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<sup>1</sup> United Nations Sanctions (Democratic People's Republic of Korea) Regulations 2006 (the Sanctions Regulations), regs 5 and 19.

<sup>2</sup> Customs and Excise Act 1996, s 203 (1)(b) & (3)(b).

[2] The Sanctions Regulation charges carry a maximum fine of \$100,000 each, and the erroneous entry charge has a maximum fine of \$5,000.

[3] On 16 March 2018 having heard submissions I reserved my decision on sentencing PAL. I now deliver the decision.

### **Background**

[4] PAL is a New Zealand registered company that manufactures aircraft. One of the aircraft it manufactures is the P-750 XSTOL. This is a multi-use aircraft that can be modified to suit the purpose for which it is required. This includes passenger and freight transport, skydiving/parachuting, surveillance, photography and firefighting work.

[5] In September 2016, it was widely reported by international media that a PAL P-750 aircraft was demonstrated at the Wonsan air show in the DPRK. As a result of the media attention Customs commenced an investigation as to how a NZ manufactured aircraft came to be in the DPRK.

[6] That investigation revealed that in 2014 PAL entered into a joint venture with Beijing General Aviation Company (BGAC). This resulted in the supply of a number of aircraft to China, one of which was the P-750 flown at Wonsan.

[7] This P-750 had been sold to BGAC as a demonstrator aircraft, arriving in China in September 2015. That same month, BGAC advised PAL the plane had been on-sold to Freesky Aviation Company Limited (Freesky), another Beijing based company.

[8] Importantly, PAL was also advised that Freesky intended to base the aircraft in the DPRK, where it would be used for tourism purposes.

[9] The aircraft came with a two year/500 flight hour warranty. Freesky received the benefit of that warranty when it purchased the aircraft.

[10] On 6 January 2016 PAL was advised of the aircraft's arrival in the DPRK.

## **The Sanctions Regulations**

[11] Pursuant to the Sanctions Regulations aircraft and their parts are defined as luxury goods, and therefore prohibited exports to the DPRK.

[12] PAL's sale of the P-750 to BGAC was not a breach of the Sanctions Regulations on the part of PAL. However, breaches of Sanctions Regulations arose when PAL, on three separate occasions, supplied warranty parts to Freesky, knowing that the parts would be sent to repair the aircraft based in the DPRK.

[13] The warranty parts, which were sent to China included a flap actuator, a digital NP indicator and a digital NP RPM indicator. The indicators are part of the cockpit instrumentation system. The last part sent was an ejector, being part of the fuel delivery system.

[14] The Customs investigation also revealed there had been an erroneous customs declaration regarding accessories sent with the aircraft when it was delivered to China. PAL failed to declare the aircraft contained two medevac stretches and a "floor plug", which when installed would allow survey equipment to be attached to it.

## **Victim Impact Statement**

[15] A Victim Impact Statement has been prepared on behalf of the Ministry of Foreign Affairs and Trade, describing the impact PAL's offending has had on the New Zealand Government and New Zealand's international reputation.

[16] The statement notes that the United Nation's Security Council's sanctions regime is the strongest action available to the international community to counter the DPRK's weapons programme, short of military intervention. Such sanctions regimes are only effective if every UN member state uses its best efforts to ensure compliance. Breaches of sanctions are scrutinised by the international community, often publicised and can impact negatively on the reputation of the breaching country.

[17] New Zealand is seen to have a reputation for being a responsible country that takes its international obligations under United Nations Security Council sanctions regimes seriously.

[18] On this occasion PAL's breaches has subjected the New Zealand Government to international scrutiny and criticism. The breach was investigated and publicised by the UN DPRK Sanctions Committee Panel of Experts. This has resulted in some countries questioning New Zealand's implementation of the sanctions regime, which has in turn caused the New Zealand Government considerable concern and required significant resources to manage the criticisms. This has been done through diplomatic missions abroad, and at key regional/international fora.

[19] Were New Zealand to have a reputation for lax sanctions implementation, this would cause commercial harm to other New Zealand companies abroad, as commercial partners may be less willing to work with them. It could also result in other countries applying export restrictions to New Zealand.

[20] The statement notes that PAL's failure to advise the New Zealand Government of the presence of the plane in the DPRK in January 2016, when it first became aware of this, meant that New Zealand's credibility and ability to manage the impact on its international reputation was diminished.

### **Customs Service's submissions**

[21] Customs, after referring to the purposes and principles of sentencing, submitted:<sup>3</sup>

...it is imperative in sentencing for offending of this kind which has risen as a result of a commercial decision that the punitive consequences go some way towards outweighing the financial benefits so that the sentence does not amount to a mere licencing fee that can be harmlessly absorbed by corporate entities who enter into financial agreements with corporations operating in the DPRK.

[22] Customs submit that the purposes of denunciation and deterrence need to be read in the context that the DPRK has been determined to be, and continues to be, a

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<sup>3</sup> Prosecutors Submissions 22 December 2017 at 3.5.

threat to international peace and security. A violation of international sanctions imposed by the Security Council needs to be condemned by New Zealand to uphold its requirements under the resolutions.<sup>4</sup>

[23] Customs, in highlighting the aggravating factors of this offending also relies on an affidavit filed by the Senior Customs Officer assigned to undertake the investigation.<sup>5</sup> The investigation was undertaken in two parts. The first related to the export of the aircraft. This did not reveal any breach of the Sanctions Regulations. The second was in relation to the export of parts, which Customs only became aware of following the receipt of information from the Ministry of Foreign Affairs and Trade. Following receipt of this information Customs identified the breaches which led to this prosecution. Customs investigating officer was highly critical of PAL in that:

- (a) they had failed to disclose information about the export of parts at the time of the initial Customs investigation (which was focused on the export of the aircraft);
- (b) they were aware of the Sanctions Regulations and the presence of the aircraft in the DPRK, but failed to notify the government of this and still sent the warranty parts to China;
- (c) they were independently aware of the aircrafts movements but failed to disclose this at the time of the initial investigation;
- (d) it appeared they were wanting to send a technician to the DPRK to install the parts; and
- (e) they were not overly co-operative with the Customs investigation.

[24] Given that aircraft parts constitute the most serious and potentially harmful type of luxury goods that can be exported, Customs submits a starting point close to the maximum penalty available should be adopted. This is due to the potential military

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<sup>4</sup> Above n3 at 3.6.

<sup>5</sup> NZ Customs affidavit dated 19 December 2017.

use of such goods, their limited availability and high value. Further, it is submitted that there should be no significant distinction for sentencing purposes between the export of an aircraft and the parts of an aircraft, while it is under warranty. It is submitted that exporting such replacement parts had the effect of making the aircraft operational.

[25] The following aggravating factors are relied upon:

- (a) the warranty parts were exported to China with actual knowledge that the aircraft was in the DPRK;
- (b) PAL made a commercial decision to maintain a commercial relationship by providing warranty parts for the aircraft, rather than complying with the Sanctions Regulations;
- (c) there were three exports over a six-month period, being repetitive offending showing a repeated disregard for the Sanctions Regulations; and
- (d) the impact the offending has had on New Zealand's international reputation.

[26] It is submitted a starting point of \$70,000 for each of the sanctions regulation charges is appropriate and that the fines should be cumulative for each export. Additionally, that there be a \$1,000 fine, cumulative on the other fines, for the erroneous export entry charge.

[27] As for mitigating factors, it is acknowledged that PAL has taken steps to ensure future compliance with the Sanctions Regulations and that the guilty pleas were entered at the first opportunity.

### **PAL's submissions**

[28] PAL acknowledges the significance of its offending and does not seek to minimise it. PAL submits that it was aware of the existence of trade sanctions in respect of the DPRK, but that it did not know the detail of the Sanctions Regulations.

[29] PAL highlight the P-750 was lawfully exported to China and nothing was done to conceal the export of the aircraft or the parts. It submits that PAL's interactions with the other parties was undertaken in a "business-as-usual" manner.

[30] While PAL was aware of the aircraft being relocated to the DPRK, it understood this was to be on a temporary basis, for tourism purposes.

[31] PAL co-operated with Customs in its investigation of the export of the P-750 to China and its subsequent on-sale to Freesky. In its view, it responded to all of Customs inquiries. It also responded to the UN Panel of Experts' investigation as to how the aircraft became to be in the DPRK. This was voluntary on the part of PAL, given there is no provision for enforcement of such a request for information. In the course of responding to queries from the Panel of Experts documentation relating to the export of the warranty parts was disclosed. It was this information that the Panel of Experts provided to the Ministry of Foreign Affairs and Trade, who in turn provided it to Customs and which then led to the second investigation.

[32] PAL believes that it complied in all ways with both the first and second Customs investigations. Prior to the conclusion of the second investigation, and before any charges were laid, when PAL became aware it may have "inadvertently breached" the Sanctions Regulations, it advised Customs of this.

[33] PAL submits that it has not benefited financially or commercially from the export of the warranty parts. These parts were provided to Freesky without charge. The value of the parts was approximately \$6,700. PAL submits that the parts themselves have no military application, and nor are they luxury goods, in the sense of being a symbol of the elite.

[34] PAL acknowledges the significance of its offending, and that at all relevant junctures it should have either known or sought advice on the detail of the Sanctions Regulations. Since these breaches came to light, PAL have created a new position within the company, namely that of a Sanctions Officer to ensure there are no further breaches of this kind.

[35] PAL notes that as a result of the initial media reporting of the aircraft being flown at the Wonsan air show and the subsequent charging of PAL, multiple inquiries have been received from concerned customers and suppliers. Some customers payments have been disrupted because of this attention.

[36] To address the position PAL has found itself in, considerable time has been spent explaining its situation to its suppliers, particularly those in the US. It is unknown, what if any, further actions may arise in respect of its relationships with US based companies and whether there may be other direct action taken by US authorities.

[37] PAL submits that the starting point submitted by Customs is too high in the circumstances of this case.

[38] It accepts a cumulative fine of \$1,000.00 is appropriate in respect of the erroneous export entry charge. In this regard, it notes that the inclusion of the two medevac stretchers and the “floor plug” was as a result of a customer request made just prior to the export of the aircraft. Both items remained in the ownership of PAL for some time, and nor were they with the P-750 when it relocated to the DPRK.

[39] In terms of the aggravating features identified by Customs, PAL submits:

- (a) The charges relate to the exporting of the warranty parts and not the aircraft itself. The warranty parts were of a relatively moderate monetary value, were civil aircraft components and had no military purpose. They were necessary for the aircraft’s safe operation.
- (b) The exporting of the warranty parts was for no additional commercial benefit. They were for warranty purposes only. Additionally, there was no active decision to breach the Sanctions Regulations and PAL’s actions were driven solely by its warranty obligations and safety concerns.
- (c) While PAL was aware that the aircraft had relocated to the DPRK it understood this was on a temporary basis. It was not until after



September 2016 that it became aware the aircraft was there on a more permanent basis.

- (d) While there were three occasions of exporting the warranty parts there was no change to PAL's state of knowledge over the period the parts were exported.
- (e) Regarding the loss and harm outlined in the Victim Impact Statement, PAL accepts that there will have been a general detrimental impact on New Zealand's reputation in the international community. However, it notes that the statement is general in nature and does not suggest that there has been any specific impact. It also notes that the statement does not distinguish between the scrutiny and criticism that may have arisen because of the presence of the P-750 at the air show, and on the other hand the export of the warranty parts.
- (f) This was a case of indirect export. The parts were sent to China and not to the DPRK. The parts were sent at a time when the aircraft was based in the DPRK but remained Chinese owned and operated.
- (g) PAL acknowledges the importance of denunciation and deterrence in terms of setting the starting points, and the implications of its offending for New Zealand's reputation and international relationships, as aggravating factors. It also acknowledges that it should have done more to familiarise itself with the detail of the Sanctions Regulations. However, it submits its offending was neither cynical, nor deliberate, and at no stage did it make an active decision to breach the Sanctions Regulations.

[40] In the circumstances, it submits that the appropriate starting point would be in the vicinity of \$20,000 for each offence, being an all-up starting point of \$60,000, before mitigating factors were determined and before consideration of the totality of the penalty.

[41] It is submitted that there are a number of mitigating factors that can be considered namely:

- (a) The appointment of a Sanctions Officer, together with a number of policy and procedural changes, including a requirement for all customers to complete End User Declarations with respect to International Trade Sanctions, regardless of the country being exported to.
- (b) Amending its sales agreement to prevent the on-sale of aircraft to the DPRK,
- (c) It now formally advises the Ministry of Foreign Affairs and Trade of all foreign aircraft sales, regardless of the country being exported to.
- (d) That it has no previous criminal history and that prior to these charges was a company with a positive international reputation.

[42] Overall it is submitted that there should be a modest discount for these mitigating factors and a full 25% reduction for the early guilty pleas.

### **PAL's affidavit**

[43] In response to the Customs affidavit, PAL filed its own response, to provide background information in respect of the charges and to respond to Customs criticisms. PAL maintains the Customs' affidavit is inaccurate and is neither balanced or fair.

[44] The specific issues identified in PAL's affidavit are:

- (a) The P-750 aircraft is not designed or intended for military use, nor is it fitted with equipment or attachments specifically designed for military use. All of the P-750's manufactured to date operate on a commercial basis for activities such as freight, passenger and skydiving use. None have been purchased by individuals for private or personal use.

- (b) Around 25 September 2015 PAL was informed that Freesky was intending to use P-750 for general aviation purposes in the DPRK. While the aircraft was to be used in the DPRK, Freesky was to remain as owner of the aircraft and that it would continue to be registered in China and supervised by the Civil Aviation Administration of China.
- (c) PAL had spoken to a Ministry of Foreign Affairs and Trade official and understood from that official that as the aircraft would not be owned or controlled by a DPRK entity and because it would only be in the DPRK on a short term temporary basis, the arrangement was acceptable under New Zealand Law and would not breach the Sanctions Regulations.
- (d) PAL had previously provided warranty parts for the aircraft while it was based in China.
- (e) Because PAL's understanding was the aircraft would be in the DPRK on a temporary basis it continued to provide warranty parts. PAL acknowledges that it should have sought formal advice regarding the issue of the aircraft temporarily being in the DPRK at all junctures, including September 2015, when it knew the aircraft was to be temporarily based in the DPRK, and prior to the provision of the warranty parts in January, May and June 2016.
- (f) Given its failure to obtain formal advice, PAL failed to appreciate the different implementation in China of the UN resolutions whereby China does not consider the export of aircraft (nor by implication their parts) to the DPRK is prohibited. PAL only became aware of this as a result of the UN Panel of Experts' report.
- (g) There was no financial benefit from the supply of the warranty parts. There was never any intention to circumvent New Zealand or International Sanctions. It was a case of PAL failing to appreciate that their actions breached the Sanctions Regulations.

- (h) At no stage did PAL allow any of its staff to travel to the DPRK to undertake any repairs on the aircraft. There was however some pressure put on PAL staff by BGAC in China for PAL's China based staff to travel to the DPRK.
- (i) Once PAL became aware of the presence of the aircraft in the DPRK it attempted, through BGAC, to see what could be done, first to remove the DPRK markings painted on the aircraft, and second, to remove the aircraft from the DPRK.
- (j) It is PAL's view that it and its staff complied fully with all of Customs requests for information and interviews. Its view is that the first investigation was ad hoc and rushed, focusing solely on the aircraft as opposed to events after the export of the aircraft.
- (k) That PAL voluntarily engaged with the UN Panel of Experts' investigation. The investigation was undertaken by way of a series of letters and email exchanges. The information communicated included details in respect of all parts supplied. This was in response to a request for information relating to technical support provided in respect of the aircraft.
- (l) When Customs second investigation was initiated, PAL was by then aware of the possibility it may have inadvertently breached the Sanctions Regulations in respect of the January and May 2016 exports. At that stage, it had not identified the June 2016 export, which was brought to its attention by Customs.

[45] As a result of the Customs investigation, PAL now appreciates its obligations under the Sanctions Regulations. Accordingly, there have been a number of policy and procedural checks adopted to mitigate any further risk that PAL originating aircraft are transferred to or operated in the DPRK, or other countries that are subjected to trade sanctions.

## **Decision**

[46] Despite the unique features of this case, an orthodox sentencing process is required. I will adopt the three-stage approach. First, I will set a starting point based on the features of the offending itself. There is no guidance to be gained from any previous cases. Second, I will adjust the starting point based on any aggravating or mitigating features personal to the defendant. Third, I will consider any discount for the guilty plea.

[47] Throughout this process I have regard to the purposes and principles of sentencing set out in ss.7 and 8 of the Sentencing Act 2002. These include the need to impose a sentence that denounces PAL's conduct, promotes accountability and deters others from engaging in similar conduct. At the same time, I must bear in mind the principle that I should impose the least restrictive outcome appropriate in the circumstances.

### *Impact of the Affidavit Evidence*

[48] The offending is fully described in the Summary of Facts. Leave was not sought by the prosecutor to file the affidavit evidence. However, once filed, it necessitated a response from PAL.

[49] Customs' affidavit, as it relates to the aggravating factors, is not accepted by PAL. PAL has explained its position and provided supporting documentary evidence to justify its response.

[50] I am not in a position to resolve the conflicts raised in the competing affidavits. A s 24 disputed facts hearing has not been sought and that is understandable given the core facts are not in dispute.

[51] The utility of the affidavits filed is that they inform me of the respective parties' views. Where they are in conflict, generally I am not able to resolve that conflict. I have accordingly determined the aggravating and mitigating factors on the basis of the agreed Summary of Facts, and being informed of the respective parties' views by way

of the background material. The one exception to this approach is where there is uncontroverted documentary evidence to support otherwise.

*Setting the starting point*

[52] The purpose of the Sanctions Regulations is to give effect to Resolution 1718 (2006) of the Security Council of the United Nations. This resolution is for the purpose of imposing an arms embargo, assets freeze and travel ban on persons involved in the DPRK's nuclear programme, and a ban on a range of imports and exports, to prohibit the DPRK from conducting nuclear tests or launching ballistic missiles.

[53] The definition of arms also includes military equipment which is defined to include such items as battle tanks, armoured combat vehicles, large calibre artillery systems, combat aircraft, attack helicopters, warships, missiles, or missiles systems.

[54] The definition of luxury goods includes such items as alcoholic beverages, bone china, carpets and tapestries, caviar, chocolate, designer clothing and furniture, fountain pens, honey and its derivatives, musical instruments, perfumes, wrist watches, cars, motorcycles, snow-mobiles, motorboats, yachts, aircraft, and their parts and accessories.

[55] The Sanctions Regulations came into force in New Zealand on 15 December 2006. The maximum penalty available for breach is \$100,000.00. The maximum penalty is available, no matter the nature of the breach, whether it relates to arms, weapons of mass destruction and missile related goods, or as in this case, luxury goods.

[56] When the purposes of the Sanctions Regulations are considered, there is a discernible scale of gravity arising from the nature of the prohibited exports. The exporting of military equipment of the type defined, as compared to items from the luxury goods schedule, for example crystal glassware, would be more serious offending and attract a higher starting point.

[57] It is a relevant consideration that the exporting of the P-750 itself was not a breach of the Sanctions Regulations. It was the presence of the aircraft at the Wonsan air show in September 2016 which attracted worldwide media interest. The damage

to New Zealand's international reputation, as described in the victim impact statement, arose in part from that incident and in part following the outcome of the Panel of Experts report. The provision of warranty parts, in breach of the Sanctions Regulations, would have contributed to the ability of the aircraft to be flown at the air show.

[58] Offending which impacts on New Zealand's international reputation will almost invariably be serious, given the potential consequences that arise for New Zealand's export community, particularly those that are involved in similar business areas to PAL. The damage to New Zealand's reputation had the potential to be both catastrophic and difficult to recover from. In this case, given the contents of the victim impact statement, catastrophic consequences appear to have been avoided. It is, however, a recorded breach which was investigated by the UN Panel of Experts, which of itself is significant.

[59] PAL's breach of the Sanctions Regulations was best described as reckless. PAL was aware of the Sanctions Regulations but had chosen not to fully inform itself of its detail. Given its knowledge of the existence of the Sanctions Regulations, a prudent exporter, knowing that one of its aircrafts was going to be based in the DPRK, whether temporarily or not, would have familiarised itself with the detail of the Sanctions Regulations. If this was beyond its internal capabilities, a prudent exporter would have sought outside advice. Obtaining such advice would not have been prohibitively expensive, time consuming, or in any way difficult.

[60] The breaches took place over a period of approximately six months and involved three separate exports. While the breaches were repetitive, there is no evidence of any change in the PAL's lack of knowledge throughout this period. PAL were ignorant of the detail of the Sanctions Regulations and that their actions were in breach of those regulations, from the beginning to the end.

[61] Because of the potentially serious impact of breaching the Sanctions Regulations, there is an obligation on exporters to be aware of the detail of the regulations, to ensure that they do not inadvertently commit an offence, for what may appear to be a relatively innocuous or inexpensive item, but which has the potential to

cause significant reputational damage to New Zealand. Just like all legislation, the Government relies on those who may be affected by it, being aware and informed of their obligations.

[62] The combined value of the parts is relatively insignificant, approximately \$6,700.00. I treat that as a neutral factor in terms of assessing the seriousness of the offending.

[63] When I consider these factors, the appropriate starting point, in my view, is a fine of \$35,000.00 on each of the Sanctions Regulations charges. The fines are cumulative.

*Aggravating factors relevant to PAL*

[64] There are no aggravating factors that need to be taken into consideration. There are however, a number of mitigating factors that can be considered.

*Mitigating factors relevant to PAL*

[65] As a corporate entity, PAL has not previously been before the Courts. It is able to call on its previous reputation of being a good corporate citizen. By international standards it would be a small to moderate sized company, employing approximately 180 personnel. It is working in a technologically advanced area, earning export dollars for New Zealand. In these circumstances I reduce each of the fines by \$1,750.00.<sup>6</sup>

*Plea of guilty*

[66] As has been recognised by the Supreme Court in *Hessell v R*, a plea of guilty is to be recognised by way of a 25% maximum reduction in sentence.<sup>7</sup> The plea of guilty on the part of PAL, came at the earliest possible opportunity and accordingly, the full 25% reduction, amounting to \$8,315.00 on each charge, is to be made.

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<sup>6</sup> This represents a 5% reduction.

<sup>7</sup> *Hessell v R* [2010] NZSC 135.



[67] Regarding Customs' submission, that there are aggravating factors, in that PAL failed to fully co-operate or disclose the relevant information at the time of the first investigation, I do not accept that has been established. To the contrary, PAL voluntarily engaged with the UN Panel of Expert's investigation, proving to it the documents that ultimately lead to this prosecution.

[68] Since the investigation, PAL has also taken steps to ensure that this type of offending does not happen again. The steps taken include appointing a Sanctions Compliance Officer, amending its sales documentation to prevent such on-sales as occurred here, and to formally notify the Ministry of Foreign Affairs and Trade of the destination of all exported aircraft. These changes to its operation are a recognition of its part in, and of the seriousness of its breach.

[69] In respect of the erroneous entry charge, that carries a maximum fine of \$5,000.00. PAL explained this offending arose as the request for the stretchers and floor plug was made just prior to the aircraft leaving New Zealand. It was an administrative oversight in failing to record these items as being included in the export. In these circumstances, and taking into account the mitigating factors I have already identified, a fine of \$1,000.00 is appropriate.

#### *Remorse*

[70] I have considered if there should be any further reduction for remorse on the part of PAL. I have concluded that while they are clearly remorseful for their recklessness regarding their obligations under the Sanction Regulations. it is not remorse of the type that would warrant a further discrete reduction.

#### *Totality*

[71] On the Sanctions Regulations charges the total fine is \$74,805.00. I have considered the overall totality of the fines and am of the view that no further reduction is required, overall it is an appropriate penalty.

[72] Arrangements for payment of the fines can be made with the registrar who can refer the matter back to me if any issues arise.

J Bergseng  
District Court Judge