



903:In-house Counsel Export Control Survival: Protecting Your Company

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Faculty Biographies

Angeline G. Chen

International Launch Services, a Lockheed Martin subsidiary and an international joint venture between Lockheed Martin and Khrunichev State Research & Production Space Center. Ms. Chen also serves as an adjunct professor with the George Mason University Law School, where she teaches a course in technology, terrorism, and national security law.

Prior to joining Lockheed Martin, Ms. Chen served as deputy associate general counsel for Information Security with the National Security Agency, and as assistant general counsel for INTELSAT. Prior to going in-house, she spent several years in private practice. Her responsibilities at these entities included the provision of legal advice in a variety of substantive legal areas, including international, commercial, regulatory, compliance, policy, and risk management.

Ms. Chen is an active member of a number of professional organizations, including the ABA, currently serving as the deputy editor of *The International Law News*, cochair of the Aviation & Aerospace Law Committee, cochair of the Law Students & New Lawyers Outreach Committee, associate editor of *The Air & Space Lawyer*, and previously as chair of the Task Force on Aerospace Law. In August of 2001, Ms. Chen was appointed to the ABA Standing Committee on Law and National Security.

She holds a JD from Villanova University School of Law and an LLM in International and Comparative Law, with distinction, from Georgetown University Law Center. She is currently an MBA candidate at the University of Maryland.

William L. Clements

William L. Clements is corporate counsel, international trade regulation for the General Electric Company. In this capacity, Mr. Clements advises GE's 13 industrial and financial business groups on U.S. laws and regulations relating to dual-use exports, munitions exports, economic sanctions, foreign boycotts, and foreign corrupt practices. In addition, he communicates the company's position on issues relating to these areas of the law to Congress and to Executive Branch agencies.

Prior to joining GE, Mr. Clements served as director for nonproliferation and export controls on the staff of the National Security Council at The White House. There, he coordinated the development of administration policies intended to stem the proliferation of weapons of mass destruction, advanced conventional weapon systems, and ballistic missiles, to ensure data security and information privacy and to support international sanctions. Prior to his service at the NSC, Mr. Clements served at the U.S. Department of Commerce, Bureau of Export Administration as the director of the office of technology and policy analysis and as the senior policy advisor to the under secretary. Mr. Clements was a member of the senior executive service.

Mr. Clements was awarded a Congressional Fellowship by the American Political Science Association, and served in the office of Senator Max Baucus, where he worked on international trade. He also has extensive experience in the regulation of civilian nuclear power and in public utility rate regulation.

Mr. Clements holds a BS from Cornell University, a JD, *cum laude*, from Suffolk University Law School, and an LLM in international and comparative law from the Georgetown University Law Center.

David S. Hanson

David S. Hanson is associate general counsel of W.W. Grainger, Inc. in Lake Forest, Illinois, which is a Fortune 300 distributor of commercial and industrial products to business to business and government markets. Grainger conducts business globally with locations, subsidiaries, agents, and representatives in Canada, Hong Kong, Mexico, Asia, Latin America, and the Middle East. Mr. Hanson's responsibilities focus on general commercial and corporate work with particular responsibilities for antitrust and regulatory compliance matters, supply chain negotiations, litigation management, and general commercial affairs. Additionally, he is responsible for international legal matters including compliance counseling, global procurement, customs, acquisitions, distributorships, and corporate and joint venture counseling.

He has participated in numerous Bar Association international activities, is a member of the Illinois and Chicago Bar Associations, and is admitted to practice before the Seventh Circuit and the U.S. Supreme Court.

He received his undergraduate degree from the University of Illinois and his law degree from Loyola University, Chicago.

Export Controls Survival for in-house counsel: Compliance and Risk Mitigation

*Angeline G. Chen
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What are export controls?

The United States, as do other nations, has laws that regulate the export and import of strategically important products and technology for reasons of foreign policy and national security. All manufacturers and exporters of these products and technologies are subject to these controls.

US companies are required, by law and regulation, to be familiar with and to abide by these regulatory controls.

What are they good for?

- Prevent proliferation of weapons of mass destruction
- Furtherance of national security objectives and requirements
- Furtherance and achievement of foreign policy objectives
- Supports war on terrorism

Why should lawyers care?

- Legal risk and exposure resulting from violations. The standard does not include intent.
- Overlap with other types of legal restrictions and obligations. *E.g.*, FCPA restrictions are parallel with Part 130 restrictions.
- Extension of risk is significant. All corporations must be aware that their subsidiaries, employees, officers/directors, partners, agents are required to understand and comply.

What is the role of the attorney?

- **Advise and guide**
- **Mitigate legal risk and liability**
- **Conduct and/or supervise investigations**
- **Assist in drafting of disclosures**
- **Assist in disseminating lessons learned**
- **Assist in identifying/implementing best practices**
- **Provide input and assistance in training**
- **Assist in audits and internal reviews**
- **Provide management interface for export/import issues and concerns**

International Consortiums, Treaties, Laws and Regulations

- Missile Technology Control Regime
- Bilateral and multilateral conventions
- Int'l Economic Emergency Powers Act
- Arms Export Control Act
- Int'l Traffic in Arms Regulations
- Export Administration Regulations
- US and UN embargoes

USG Agencies

- **U.S. Department of State**
 - Directorate of Defense Trade Controls
- **U.S. Department of Commerce**
 - Bureau of Industrial Security
- **U.S. Department of Defense**
 - Defense Technology Security Administration
- **U.S. Department of the Treasury**
 - Office of Foreign Assets Controls
 - Bureau of Alcohol, Tobacco and Firearms
- **U.S. Department of Homeland Security**
 - U.S. Customs Bureau
 - Bureau of Alcohol, Tobacco and Firearms
- **U.S. Department of Energy**
- **Nuclear Regulatory Commission**

Penalties for Failure to Comply

- | | |
|---|--|
| • <u>Corporate</u> | • <u>Individual</u> |
| – Fines up to \$1m per violation | – Fines |
| – Forfeitures | – Imprisonment up to 10 years |
| – Loss of export privileges (debarment) | – Disciplinary action, up to and including dismissal |
| – Loss of facility clearances | |

Definitions

Export

The transfer or disclosing of technical data or the transfer of a defense article, or the provision of defense services, to a foreign person or entity in any manner, whether within the United States or abroad (includes oral, visual, fax, phone, e-mail, etc.)

Technical Data

Information which is required for the design, development, production, manufacture, assembly, operation, repair, testing, maintenance or modification of commodities. May include information in the form of blueprints, diagrams, formulae, tables, engineering designs, specifications, manuals, instructions, drawings, photographs, plans and documentation.

Defense Services

The furnishing of assistance (including training) to foreign persons, whether in the US or abroad, in the design, development, engineering, manufacture, production, assembly, testing, repair, maintenance, modification, operation, demilitarization, destruction, processing or use of defense articles.

Foreign Person

A person who is NOT a citizen or lawful permanent resident of the United States of America.

- Corporations/businesses/partnerships incorporated to do business in the U.S.
- Includes embassies or foreign consulates
- Includes international organizations

Applies to all tiers: e.g., employees, consultants, subcontractors.

Infrastructure of Controls Governing the Business Environment

Controls Infrastructure

Authorizations/Approvals

Specific licensing arrangements ensure that impacted business activities and transactions meet the requirements of U.S. laws and regulations by stipulating the rules of operation and evidencing authorization and approval for covered activities.

MLA

TAA

DSPs

Controls Infrastructure

Internal Controls

Internal control plans and programs ensure that specific business entities meet the requirements of applicable export and import control laws as well as specific license requirements by defining the internal procedures of handling and storage of technical data, as well as technology transfers and business activities.

TTCP

**Corporate
Policies**

ICP

Manufacturing and Technical Assistance Agreements

What are they?

MLAs and TAAs are licensing agreements that are reviewed and approved by the U.S. State Department, Office of Defense Trade Controls (ODTC). MLAs and TAAs approve the relevant Statement of Work and define the rules of engagement for permissible transfers of technical data and provision of defense services pursuant to a defined scope of business activity or manufacturing effort.

All parties to the MLA/TAA must comply with the license and associated provisos in order to do business.

Technology Transfer Control Plans

What are they?

TTCPs are license-specific internal control plans that are required under the terms of a TAA.

- Provides specific requirements for handling of technical data and information
- May and often do vary between licenses
- In most cases, must be negotiated with and approved by the Defense Technology Security Administration prior to the provision of technical assistance or the export of technical data.

Internal Control Plans

An internal control plan (ICP) is a compilation of formalized policies and procedures designed to detect, deter and prevent employee and company violations of export control laws and regulations. An ICP identifies the company's risk profile in this area, and officially incorporates core principles into the company's compliance program.

Where do I start?

Know your stakeholders!

- | | |
|--|--|
| <ul style="list-style-type: none">• Internal business<ul style="list-style-type: none">– Mission– Organizational structure– Departments– Functions– Responsibilities• Internal individuals<ul style="list-style-type: none">– Employees– Governance individuals– Agents/Representatives– Consultants– Investors | <ul style="list-style-type: none">• External<ul style="list-style-type: none">– Customers (both actual and potential)– Vendors and suppliers– Distribution channels• Corporate Partners<ul style="list-style-type: none">– Joint ventures– Strategic alliances• US Government<ul style="list-style-type: none">– Congress– Regulatory agencies• Foreign governments |
|--|--|

Know your obligations!

- | | |
|---|--|
| <ul style="list-style-type: none">• Basic working knowledge of export/import controls• Requirements• Implementation• Recordkeeping | <ul style="list-style-type: none">• Identification of responsible individuals and departments within the organization• Identification of cognizant USG agencies and scope of jurisdiction |
|---|--|

Know the hotspots and red flags!

- Screening/denied parties
- Unusual transactions
- Unusual parties
- “High risk” data and information
- Nature of services being provided or received
- Nature of transaction (including payment method)
- Transaction flow
- Corporate cultural mindset
- Reluctance of customer/purchasing agent to provide information
- “Inconsistencies”

Know the weak links!

- Computers and databases (improper access or use)
- Human error (carelessness, negligence)
- Lack of knowledge (does not know rules or regulations)
- Shipping errors (wrong item in package, wrong package, switched package, incomplete info)
- Misinterpretation (know rules but misunderstood or misapplied)
- Travel (handcarry, laptop not on license)
- Tracking (failure to track value, quantity, time limits, records)

Internal Control Plan and Compliance Program

ICP Basics

- Make sure the ICP fits your company
- Make sure the ICP is a flexible, evolving document
- Make sure the ICP is manageable
- Ensure senior management supports the ICP

Internal Control Plans (Basic Components)

- Clear statement of management policy
- Export control function infrastructure and delegations of authority/Identification of responsible officials
- Basic export control requirements
- Continuing training and awareness enhancement programs
- Screening procedures for customers & transactions
- Internal review/audit process
- Notification and reporting

Management Policy

Objective: To convey a clear commitment of compliance with export controls from senior management to all employees.

- **Prepare and distribute a senior management policy statement.**
 - *Under no circumstances will sales be made/activities conducted that are contrary to U.S. export regulations.*
 - *A point of contact for any questions concerning the legitimacy of a transaction or potential violation*
 - *A description of the penalties applied in instances of compliance failure and/or violation*
 - *Express commitment of company to compliance*
- **Provision of adequate money, personnel, support and backing to make compliance initiatives and efforts effective.**

Export Control Infrastructure

Objective: To ensure that all compliance-related functions, duties and responsibilities in the company are clearly identified and assigned, that POCs are known and that this information is kept current.

- **An organization chart identifying responsible individuals and general export control responsibilities.**
- **Personnel with export control responsibilities should have commensurate authority to execute those responsibilities.**
- **Contact information for responsible officials.**
- **Ensures coordination, consistency, efficient monitoring and institutional knowledge.**

Basic Requirements

Objective: To ensure a general understanding of export control requirements sufficient to allow employees to identify potential and actual issues, including violations.

- **Provide appropriate levels of information:**
 - *New employee orientation*
 - *Training (recurring)*
- **Make information accessible**
 - *In-house publications*
 - *Procedural manuals and internal control plans*
 - *Intra-company website or database*

Training and Awareness Enhancement

Objective: To ensure training and education opportunities is provided, on a regular basis, to all employees involved in export-related activities.

- Orientation training for new employees and transfers.
- Should be recurring and periodic, as well as as needed.
- Qualified trainers.
- Appropriate formats:
 - Formal/structured
 - Verbal exchanges
 - Written memoranda and guidance

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Screening Procedures

Objective: To ensure prevention of prohibited commercial contact with targeted countries, individuals and entities.

- **Appropriate screening procedures (who, what and why)**
 - **Customers**
 - **Transactions**
 - **Contracts**
- **Methods**
 - **Interdiction software**
 - **Manual screening (should allow for multiple checks)**
- **Information (who collects, what is collected, what gets screened)**
- **When screening should be conducted**

Notification

Objective: To ensure that all exports and re-exports are conducted in accordance with applicable laws, regulations and policies.

- **Clear and publicized process for notification of appropriate agencies in the event of questionable, unauthorized or illegal activities.**
- **Internal investigatory processes and guidelines.**
- **Reporting requirements relating to third parties.**

Build your toolkit.

- **Guidance**
 - DTC Guidelines
 - Nunn-Wolfowitz Task Force Report (best practices)
 - DoC Export Management Systems

- **Management System**
 - Creates structure
 - Ensures consistency
 - Streamlines procedures
 - Demonstrates quality management
 - Reduces risk of violation

And when things go wrong . . .

What do you do when you have a violation?

Voluntary disclosures (ITAR § 127.12, EAR § 764.5)

- Limits potential harm to US national security and foreign policy
- Avoids/mitigates fines, penalties, suspension of export privileges
- Eliminates appearance of criminal behavior, intent, cover-up
- Demonstrates willingness and intent to comply
- Indicates export knowledge or sophistication
- Facilitates corrective action to avoid repetition
- Strengthens compliance program
- Provides lessons learned for better training

Compliance programs are a win-win solution.

- Companies must explicitly make export/import compliance a priority.
- Companies must devote adequate resources to maintain an effective export compliance program.
- Companies must remedy errors with their export compliance program immediately.
- Companies need to review export regulations regularly and remain aware of any changes that might affect their products or services.
- Companies must make voluntary disclosures when situation requires it.

U.S. International Trade Controls – A Primer for Corporate Counsel

***ACCA Annual Meeting
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William L. Clements
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General Electric Company



New Development



NYC PENSIONS TARGET GE, CONOCO BUSINESS IN IRAN By By Chris Sanders, Reuters English News Service, 2/10/2003

New York City's pension fund chief said on Monday he wants General Electric Co., Halliburton Co., and ConocoPhillips to end operations in countries that sponsor "terror," such as Iran and Syria. City Comptroller William Thompson, in a statement, accused GE(GE.N), the oil services company Halliburton (HAL.N) and the No. 3 U.S. oil company, ConocoPhillips (COP.N), of possibly hurting shareholder value, citing their sales and services in "terrorist-linked" countries. The \$31 billion pension funds for New York City's police and firefighters will sponsor resolutions that ask the companies to review those businesses

Export Administration Regulations (15 CFR Parts 730-774)

- ✦ Control the export to certain countries of products identified on the Commerce Control List (15 CFR Part 774) and specific information ("technology") necessary for the "development", "production" or "use" of those products.
- ✦ "Technology" includes "technical data" and "technical assistance.
- ✦ "Software" specially designed for the "development", "production" or "use" of certain products identified on the Commerce Control List (15 CFR Part 774) is similarly controlled.
- ✦ All U.S. products and technology are "subject to the EAR" and, therefore, may be controlled for export to embargoed entities or to entities subject to Denial Orders.
- ✦ Prior Government approval, Individual Validated Licenses, required for certain transfers, others may require written assurances from end-users.
- ✦ Transfer of technology to foreign national within the U.S. "deemed" to be an export to the home country of the recipient.
- ✦ Allowing foreign nationals, wherever located, access to computer files containing U.S. technical data is also controlled.

Office of Foreign Assets Control (31 CFR Parts 500-597)

- ✦ Generally prohibit "U.S. persons" from exporting goods, technology or services to an embargoed country, to the government of an embargoed country or to an agent of that government.
- ✦ Also prohibit "U.S. persons" from engaging in any transaction in which any Cuban national or entity, wherever located (except Cuban nationals lawfully within the U.S.), the Government of Cuba or any agent acting on its behalf has any interest, direct or indirect.
- ✦ Iran, Sudan, Libya and Iraq regulations define "U.S. person" as U.S. nationals, permanent resident aliens or corporations.
- ✦ Cuba regulations add the foreign controlled subsidiaries of U.S. corporations to the definition of "U.S. person".
- ✦ Scope of affected transactions very broad and includes all financial transactions as well as the support of a sales transaction, e.g., brokerage, common carriage, insurance or financing.
- ✦ Facilitation of a transaction that would be prohibited if performed by a U.S. person is also prohibited.

Broad Concepts Left Undefined in Regulations

International Traffic in Arms Regulations (22 CFR 120-130)

- ✦ Control the transfer of any ITAR-controlled (munitions) technical data or software to a foreign national, wherever located.
- ✦ "Technical Data" defined as information required for the design, development, production, manufacture, assembly, operation, repair, testing, maintenance or modification of defense articles.
- ✦ Generally, defense article includes all components, parts, accessories, attachments and associated equipment for items contained on the U.S. Munitions List (22 CFR 121).
- ✦ Anyone who exports defense articles must register with the Department of State.
- ✦ Controlled "Software" is that directly related to defense articles.
- ✦ Providing "Defense services" is similarly controlled.
- ✦ "Defense Service" defined broadly to include furnishing assistance relating to a defense article or military training.
- ✦ Prior U.S. Government approval necessary for all transfers.

All Transfers to non-U.S. Nationals Strictly Regulated

Overview - Scope of U.S. Regulations

Controls on Products – U.S. Regulations reach:

- All direct exports of products, software, technical data or services from the U.S.
- Re-exports of U.S. products, software and technical data from any location
- Foreign manufactured products containing U.S. origin raw materials, components, software or technology.

Controls on Business Activities:

- "U.S. Persons" may not engage in any sales, service or financial transaction involving an embargoed country, a designated representative of an embargoed country or any sanctioned entity/individual.
- "U.S. Persons" may not facilitate any transaction involving an embargoed country or sanctioned entity/individual.
- "U.S. Persons" may not engage in any sales, service or financial transaction with any national of Cuba, wherever located.
- "U.S. Persons" may not deal in any product of Cuba.
- No person, regardless of nationality may engage in the transshipment of U.S. origin products to embargoed countries (3rd country supplier placing an order on a US manufacturer to fill an order in an embargoed country)
- No "U.S. Person" may knowingly support a project to develop weapons of mass destruction or ballistic missiles in certain countries.

Technology Controls

What is controlled: technology and technical data related to:

- ✦ military/munitions items,
- ✦ design, production and use of certain dual-use products and materials to certain countries and their nationals, wherever located
- ✦ certain manufacturing processes to certain countries and their nationals, wherever located

How is it controlled: all transfers of controlled technology to:

- ✦ Anyone - customers, contractors or suppliers - located outside the U.S.
- ✦ Employees who are not U.S. nationals or permanent residents, located within or outside the U.S.
- ✦ Non-U.S. employees of customers, contractors or suppliers located within or outside the U.S.
- ✦ Company operations located outside the U.S.

Uncontrolled access to a “Data Rich” Environment Could be Deemed to be a “Transfer”

Product, Software & Tech Data Licensing

Summary

- ✦ All exports from the U.S. are controlled
- ✦ All reexports of U.S. origin product, technology and software are subject to U.S. regulations
- ✦ EAR - Need for an individual export license is determined by the combination of the technological sophistication of the product and the country of final destination (as well as all transshipment countries)
- ✦ ITAR – All transfers require a license
- ✦ License exceptions are available under EAR, very limited under ITAR
- ✦ EAR99 items generally do not require license
- ✦ Licensing requirements may extend to activities incidental to the export: brokerage, transportation, insurance, financing, facilitation.....

Critical Distinction Under EAR: Transshipment vs. Re-export from 3rd Country

Countries of Concern

Countries

Cuba – Unilateral U.S. embargo, reaches foreign controlled subsidiaries of U.S. corporations
 Iran - Unilateral U.S. embargo, limited reach
 Sudan - Unilateral U.S. embargo, limited reach
 Libya - Unilateral U.S. embargo, limited reach

Restrictions

- ✦ U.S. Persons - All sales transactions and incidental activities to countries and individuals and entities designated by USG as acting as agents of listed foreign government
- ✦ Reexports of many U.S. products, software and technology – For Cuba and Libya all U.S. items restricted
- ✦ U.S. Person – no dealings with Cuban nationals anywhere in world
- ✦ U.S. Person – no dealings in property in which Cuban national/entity has an interest
- ✦ Import ban

Other Countries

Angola/UNITA held areas – Limited U.S. & E.U. sanctions
 Burma – Limited U.S. sanctions – more may be coming

Definition U.S. Person

“U.S. Person” Includes:

- ✦ U.S. Corporations and all their employees, regardless of location and nationality
- ✦ U.S. Nationals
- ✦ U.S. Permanent Resident Aliens, I.e., Green Card Holders
- ✦ Persons Located in the U.S.
- ✦ Branch Offices of U.S. Corporations
- ✦ For Cuba – all controlled foreign subsidiaries and all of their employees

Cuba: Watch Out for Canadian, E.U. & Mexican Blocking Statutes

Export of a Service by a U.S. Person

Financial Services:

- ◆ All consumer or commercial finance transactions, direct insurance or reinsurance (including claims payment), project finance, leasing or other financial transaction involving, directly or indirectly:
 - ◇ Any private or public entity in Cuba, Iran, Libya, Sudan or Iraq.
 - ◇ Any Blacklisted agents of Cuba, Iran, Libya, Sudan or Iraq, wherever located.
 - ◇ Any national of Cuba, wherever located (except those lawfully in the U.S.).
- ◆ Direct insurance or reinsurance covering risks or property in Cuba, Iran, Libya, Sudan or Iraq.
- ◆ Brokering, supporting or facilitating any of the above.

Technical Services:

- ◆ On-line customer product support
- ◆ On-line marketing tool/design analysis
- ◆ Product/system design services

***U.S. Person - U.S. corporations, nationals and permanent resident aliens [For Cuba, add controlled foreign subsidiaries]**

Facilitation

Facilitation: Allowing or Assisting a Non-U.S. Person to Do Something That Is Prohibited to a U.S. Person

- ◆ Exercising any management or control of any transaction involving a non-U.S. Person (including a controlled foreign affiliate) that would be prohibited to a U.S. Person
- ◆ Supporting a transaction involving a non-U.S. Person (including a controlled foreign affiliate) that would be prohibited to a U.S. Person
 - e.g., Brokering, project/sales financing, extending financial reserves to cover insurance/reinsurance exposure, providing financial guarantees, insurance or reinsurance, centralized (U.S.) business/transaction support software functionality, B-2-B exchange service involving embargoed entity
- ◆ Referring a contract/order/inquiry to a foreign affiliate or other non-U.S. Person that the U.S. entity cannot perform
- ◆ Changing operating procedures of a foreign affiliate in order to facilitate transactions that would be prohibited to the U.S. entity.
- ◆ U.S. Persons may not participate in or support any transaction involving Iran, Libya, Sudan or Iraq – including product sales/service, insurance, credit, leasing, financing, etc..

Offshore Transactions Must Stay Offshore... All Involvement of U.S. Persons is Prohibited

Facilitation

Examples:

- Approve, facilitate or guarantee the performance by other persons of transactions or contracts which are prohibited.
- Perform contracts (including warranty obligations) relating to prohibited activities.
- Be operationally involved or participate, directly or indirectly, in the performance of contracts.
- Make new investments, asset commitments, or loans in relation to property or entities owned or controlled by the government of the restricted country.
- Undertake planning or supervision of contracts with restricted countries.
- Otherwise engage in any action that facilitates a prohibited action.
- Participate in adjustments to corporate policy to facilitate any transaction.

Facilitation

U.S. Regulations: Facilitation; Change of Policies and Procedures; Referral of Business Opportunities Offshore.

[A] Prohibited facilitation or approval of a transaction by a foreign person occurs, among other instances, when a United States Person:

- (A) alters its operating policies or procedures, or those of a foreign affiliate, to permit a foreign affiliate to accept or perform a specific contract, engagement or transaction involving (an embargoed country or its government) without the approval of the United States Person, where such transaction previously required approval by the United States Person and such transaction by the foreign affiliate would be prohibited by this part if performed directly by a United States Person or from the United States;
- (B) refers to a foreign person purchase orders, requests for bids, or similar business opportunities involving (an embargoed country or its government) to which the United States Person could not directly respond as a result of the prohibitions contained in this part; Or
- (C) changes the operating policies and procedures of a particular affiliate with the specific purpose of facilitating transactions that would be prohibited by (these regulations) if performed by a United States Person or from the United States.

See 31 CFR 560.417 – Apply to All Embargoed Countries

Facilitation

U.S. Regulations: Facilitation by a United States Person

- (a) ... Activity of a purely clerical or reporting nature that does not further trade or financial transactions with (an embargoed country or the government of an embargoed country) is not considered prohibited facilitation.
- (b) To avoid potential liability for U.S. persons under this part, a U.S. parent corporation must ensure that its foreign subsidiaries act independently of any U.S. person with respect to all transactions and activities relating to the exportation or re-exportation of goods, technology or services between (an embargoed country) and any other location including but not limited to business and legal planning; decision making; designing, ordering or transporting goods; and financial insurance and other risks.

See 31 CFR 538.407 – Apply to All Embargoed Countries

Business Partner Screening

Need to Screen:

- ◆ **Customers**
 - Pre-approved customer list: screen each new customer against customer list and screen entire customer list against changes to blacklist as published.
 - Order fulfillment contemporaneous with order taking - screen when order taken.
 - Order fulfillment follows order taking by some significant period of time - screen twice, when order taken or negotiations begun and again when product shipped, service provided, or deal closed.
- ◆ **Suppliers**
- ◆ **Business Partners**
- ◆ **Contractors**
- ◆ **Employees**

**20,000+ Individuals/Entities on Various Government Sanctions Lists
– 12,000+ Designated as Terrorists**

Legal Requirements for Screening

U.S. Lists:

- U.S. Persons prohibited from engaging in any financial transactions with certain designated individuals/entities. {OFAC Regulations - 31 CFR Part 500 - 598 – Criminal and Civil Penalties}
- U.S. Persons prohibited from facilitating or otherwise supporting prohibited transactions performed by non-U.S. persons. {OFAC Regulations}
- Financial assets of certain designated individuals/entities frozen and must be transferred to control of U.S. authorities. {OFAC Regulations}
- Prohibition on engaging in export transactions with certain designated individuals/entities. {Export Administration Regulations (EAR) 15 CFR 730 - 774 – Criminal and Civil Penalties}
- Prohibition on financing, facilitating or otherwise supporting export transactions with certain designated individuals/entities. {OFAC Regulations}
- Global prohibition on transferring to certain designated individuals/entities items or technology controlled by U.S. export controls. {EAR}
- Prohibition on sale of munitions items to certain designated individuals/entities. {International Traffic In Arms Regulations – 22 CFR 120-130 – Criminal and Civil Penalties}
- USA Patriot Act and implementing regulations require US financial services companies to screen all customers against all US Government lists.

European, Canadian and Australian Lists:

- Prohibition on financial transactions with designated individuals or entities.
- Freezing of financial assets of designated individuals or entities.

**Absence of Legal Exposure Does NOT Eliminate Reputational Risk
- All Names are Red Flags**

Operational Issues - Digitization

- ✦ Technology content of product/information delivered via internet or information shared via intranet (e.g., Lotus Notes Quickplace™)
- ✦ Identity/nationality of customers and suppliers (including reverse auctions)
- ✦ Business model: B2B Exchanges – brokering or facilitating prohibited transactions or transactions involving embargoed entities (brokerage vs. common carriage)
- ✦ Exposure of on-line auctions for facilitating transactions – registration requirement if auctioned product is munitions item.
- ✦ Export of a technical service or technical assistance – on-line help desk - marketing tool vs. technical advice
- ✦ Export of a financial service – insurance, credit, leasing or financial advice
- ✦ Referral of orders/inquiries from embargoed entities to subs not affected by US regulations
- ✦ Internal business support applications hosted on intranet used by foreign subsidiaries to support sanctioned transactions – location of server, nationality of host

Operational Issues - Digitization

Internet Design/Operation Issues:

- ✦ Information content on server(s)
- ✦ Access control for trade controlled technical information
- ✦ Physical location of server
- ✦ Nationality of entity controlling/hosting server(s)
- ✦ Nationality/employer of individuals maintaining server(s)
- ✦ Customer/supplier screening – browser login
- ✦ Automatic routing to offshore servers
- ✦ Use of wizards – technical service?

Intranet Issues - Controlled Technical

Information/Facilitation:

- ✦ Physical location of server
- ✦ Physical security for server
- ✦ Software safeguards – e.g., location and security of backup file copies
- ✦ "Quickplace"™ Administrator must be U.S. person
- ✦ Access authorization by U.S. person
- ✦ Password reset by U.S. person
- ✦ Support of operations or transactions of foreign subsidiaries with income streams from embargoed countries

Operational Issues - Digitization



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New software pinpoints location of web users

By Matthew Leising in San Francisco - Aug 01 2001

There is an old joke that, on the internet, "no one knows you are a dog". Now, new software will make it possible for you to be sniffed out.

"Geo-location software", the next wave in collecting information from on-line users, traces backwards the connection route established by an on-line user, locating down to the city where a person is logging on.

The software promises significant implications for a wide range of industries. But the controversial new product is also raising concerns about on-line privacy.

"We have this basic engine that tells our customers where their customers are," says Cyril Houri, chief executive and founder of Infosplit, a geo-location company. Other companies involved in geo-location development are Quova and Digital Envoy. All three are privately owned.

New Government Enforcement Standard?

Operational Issues - Digitization

B2B Exchanges: Facilitation of Transaction Prohibited to U.S. Person

Issues:

- ◆ Marrying un-embargoed supplier with embargoed customer
- ◆ Marrying embargoed supplier with un-embargoed customer
- ◆ Facilitating transaction involving embargoed party in any supporting role – insurance, common carriage, etc.
- ◆ Level of direct and knowing involvement in transaction
- ◆ Intentional blinding
- ◆ Physical location of server
- ◆ Nationality of exchange provider and its employees
- ◆ Referral of transaction involving embargoed entity to 3rd party not subject to U.S. law – including subs

High Value-Added Improves Revenue Stream Also Enhances Exposure

Other Resources

- ◆ Grist for the Litigation Mill in U.S. Economic Sanctions Programs, Stanley J. Marcuss. 30 Law & Pol'y Int'l Bus. 501 (Spring 1999).
- ◆ "If Property Rights Were Treated Like Human Rights, They Could Never Get Away with This": Blacklisting and Due Process in U.S. Economic Sanctions Programs, Peter L. Fitzgerald. 51 Hastings L.J. 73 (November 1999).
- ◆ Can Helms-Burton Be Challenged Under WTO?, John A. Spanogle, Jr. 27 Stetson L. Rev. 1313 (Spring 1998).
- ◆ Department of Commerce, Bureau of Export Administration Website: <http://www.bis.doc.gov/>
- ◆ Department of the Treasury, Office of Foreign Assets Control Website: <http://www.treas.gov/ofac/>
- ◆ Department of State, Office of Defense Trade Controls Website: <http://www.pmdtc.org/>
- ◆ Society for International Affairs (ITAR Training) Website: <http://www.siaed.org/>

Export Controls Primer

GRAINGER®

EXPORT CONTROLS PRIMER
Building Awareness of Issues and Obligations

ACCA Annual Meeting, October 2003

David Hanson, Associate General Counsel, W.W. Grainger, Inc.

Export Controls Primer

Understanding Risk Areas

Primarily Legislation - Not Case Law

- Export Administration Regulations
(EAR - CFR 730 et seq Bureau of Industry and Security
"BIS")
- Focus of Legislation
 - Ten general prohibitions
 - Dual use items
 - End use controls
 - Re-exports
 - Technology
 - Denied persons
 - "Deemed" exports
 - Freight forwarders
 - Licensing / License exceptions
 - Record keeping

Export Controls Primer

Understanding Risk Areas

Ten General Prohibitions - 15 CFR 736

- People - Individuals and Entities
- Products
- Places - Dealings with Prohibited Countries
- Re-export
- Technology and Software
- Deemed exports
- Shipments to/from/through prohibited countries
- Licensing
- Support of Proliferation Activity
- Proceeding with knowledge of violation or possible violation

Export Controls Primer

Understanding Risk Areas

Sanctions and Embargoes - A Complex Web

- Jurisdiction - applies to U.S. persons worldwide, and if owned or controlled by U.S. entity.
- 31 CFR Chapter V
 - Office of Foreign Assets Control - OFAC, Dept of Treasury
 - Cuban Assets Control Act
 - Embargoes administered by OFAC - Libya, Iran, North Korea, Sudan
 - Country or Entity sanctions - prohibitions dealing with parties, e.g., Denied Persons List, Entity List, Specially Designated Nationals List, Debarred List
 - Watch Canadian and Mexican subsidiaries for counter embargoes, FEMA for Canada

Export Controls Primer

Understanding Risk Areas

Sanctions and Embargoes continued

- BIS, State Dept, and Treasury Depts have varied jurisdictions
 - Specially Designated Nationals "SDN" = Dept of Treasury
 - Debarred Parties = State Dept
- Foreign Corrupt Practices Act
- ITAR - International Traffic in Arms Regulations
22 USC 2771, 22 CFR 120
 - goods, services, and technology which may have military application
 - any good made for military specifications - even if available in general market

Export Controls Primer

U.S. Anti-Boycott Regulations

- 15 CFR 760 and Internal Revenue Code 93-999A
- Enforced by BIS and Justice Department for export controls - IRS for tax purposes
- Severe criminal and financial risks, and reputational damages
- Potential loss of government contractor status

Export Controls Primer

Collateral Post 9/11 Legislation

- Patriot Act - Antiterrorism legislation focuses on:
strict employment screening, new visa procedures,
money laundering assessment techniques, especially
enhanced “know your customer” duties including links
to OFAC
- New Cargo inspection procedures for importers
 - Freight forwarder requirements
 - “Know your Supplier” and supply chain compliance
issue (CTPAT)
 - Stepped up audits by Customs officials
- Creates compliance vulnerabilities for Customs
issues

Export Controls Primer

How to Assess Your Company's Vulnerability

- Focus on risk assessment within your organization
 - Develop awareness of core issues
 - Interview employees and service providers
 - Understand products, customers, and suppliers
- Look at situation holistically - Suppliers to products to
employees to dealers to customers
- Propose an appropriate compliance program

Export Controls Primer

Understand Chief Export Selling Risks

- Product classification
 - ECCN (Export Commodity Control Number), on the CCL or EAR 99
 - Know your Company's product ECCNs
- End user
 - Know your customer or distributor
- End use sanctions
 - Know country destination, persons and entities
- Broad Sarbanes-Oxley obligations
 - Need to have compliance plan in place by 2004

Export Controls Primer

How to Assess Your Company's Vulnerability

- Understand how your Company goes to market internationally
 - Customer direct or by distribution partners
 - Licensing
 - Joint Venture
 - Internet
 - Manufacturing or Production
 - Franchise or Dealership
 - Acquisition
- Perform due diligence of your distribution chain associates, especially in an acquisition context to avoid assuming liabilities
- Develop a supplier/distributor questionnaire to build a compliance due diligence record
- Review Foreign Corrupt Practices compliance

Export Controls Primer

Understand Customer Sales Channels and Order Inputs

- Where do orders come from?
 - Walk ins
 - Telephone/Fax/Email
 - Licensees
 - Internet - Company website
 - Internet marketplace
 - Company sales representatives
 - Independent sales reps or agents
 - Joint ventures
 - Correspondent bank dealings
 - Overseas trade shows

Export Controls Primer

Understand Customer Sales Channels and Order Inputs

- EAR requires that your firm “know its customers” and be aware of likely end users, end use, and final destinations of products
- Sales of products or their re-export to certain persons and places are prohibited
- Export order definition
 - An export order is (i) a shipment or transmission of items subject to EAR out of the United States, or (ii) a release of technology or software in the United States to a foreign national of a country subject to EAR.
 - Evaluate whether you actually have export orders - many Companies do not know they have export orders - they believe if it is delivered to freight forwarders, it is not export
 - Develop and implement Export sales terms and conditions to address risks

Export Controls Primer

Know Your Customers' Requirements

- EAR requires that steps be taken to “know your customers”, screen them, and the end use and destination of products. Supplement 3, Part 732, EAR
- Look for “Red Flags”
Examples:
 - Customer is reluctant to give information about end use, end user, ultimate destination, or delivery dates
 - Customer will pay cash for expensive item or decline any information about performance, operations or warranties
 - Shipping and packaging are unusual
 - Product is incompatible with country specifications or needs
- Review BIS website - www.is.doc.gov for daily updates and limits

Export Controls Primer

Analyze your Company's Products, Suppliers, and Supply Chain

- Understand your Company export products
 - Required to classify products for coverage by EAR
- Classify your products according to Export Commodity Control Number (ECCN) - will avoid potential fines and export delays
- Have process to acquire and update licensing requirements and exceptions, and acquire product information from Suppliers so export sales documentation can be accurately completed
- Incorporate ECCN information in your purchasing agreements - have Supplier indemnify accuracy of
- Be aware that combinations of products may cause vulnerability
- Retain records of such classification for five (5) years from date of export

Supply Chain Issues

- Enlist support of purchasing department, engineering, and export consultants or reputable freight forwarders to properly classify products
- Have agreements with export freight forwarders, including indemnifications to ensure that Shipper Export Declarations (SEDs) and product certificates of origin are accurate so that NAFTA certificates, etc. are properly filed
- Avoid blanket Powers of Attorney with forwarders providing minimal responsibility for forwarders
- Changes to export documentation rules make exporters, not freight forwarders responsible for compliance with EAR ... Principal Parties in Interest rules and SEDs - verify information
- A false statement in a SED may be a criminal violation