



International Operations: Managing The Risks

BY JEFFREY L. SNYDER

COMPLIANCE management is what lawyers do when they are not engaged in crisis management. It is no less important and not much easier. Having good compliance programs in effect is half the battle; but keeping them up to date, customizing them to the business, keeping them from stifling legitimate business and avoiding complacency all require constant attention.

Incomplete or ineffective compliance with a group of U.S. laws that affect international operations can create unwanted exposure.¹ The chances of running afoul of the export control laws, the trade embargoes, the Foreign Corrupt Practices Act (FCPA), and yes, even the Antiboycott Law, are greater now than ever before.²

As the U.S. Government struggles to find its role in the post-Cold War era, old laws are being shaped and twisted to fit new situations. This creates uncertainty for companies where prudence calls for adequate planning and anticipation in securing compliance.

Consider the following:

- A product or some technology is exported and no one knows whether prior authorization is required.
- A related offshore company resells U.S. products and no one knows whether prior authorization is required for the resale.
- A business unit responds to a request about whether the company does business in or with Israel.
- A business unit hires an agent to sell to a foreign government which, unknown to you, bribes the official responsible for the business.
- A business unit hires foreign nationals from China or Russia to work in U.S. operations.
- Company officials travel with laptop computers containing software with encryption features.
- A business unit makes a sale to a European company that is in reality a front company for Baghdad.

Each of these events is (or could be) a violation of U.S. law. Even seemingly minor violations can be treated seriously. The range of penalties includes

not only fines, but also debarment from government contracting, denial of export privileges, and in some cases, criminal penalties.

The most common technique to avoid or prevent violations is an internal compliance program. Can violations be prevented? Sometimes, but not all of the time. Mistakes are inevitable because full compliance with the laws in this area is virtually impossible.³

A colleague of the author once told him that full compliance with environmental laws is impossible because the expense would bankrupt any company. For international operations, it is not so much the expense as the sheer number of rules, their complexity, how fast they change and the inconsistency of the underlying U.S. policy objectives. Compounding this is the multitude of U.S. Government agencies involved in the investigation and enforcement of these rules.

This article reviews a selected list of issues in managing the risks and exposure faced by a company in its international operations. The list is divided into three topics: (1) managing compliance; (2) managing mistakes; and (3) issues for the future.

*Does the internal compliance program work?*⁴ This question can be answered from several perspectives. The first test is asking, "Does it help prevent violations?" Will one of the enforcement agencies find something that slips through the cracks of the program? For instance, the U.S. Customs Service (Customs) now routinely screens shipper's export declarations (SEDs) by running the data through a special "filter." Comparing commodities and values, the program will pull out typographical errors, but will also identify possible violations. The Commerce Department has initiated hundreds of audits and many enforcement actions through the SED review program.⁵

Another way to test the program is to ask whether it is likely to be considered a mitigating factor should a violation ever occur. A compliance program can be a mitigating factor when the government hands out penalties.⁶ Not just any program will have this power. The program must be real and well-functioning.⁷ Does it have the support of senior management?

What does it cover? Depending on the size and type of company, the areas to cover will vary. For most companies, however, a few are essential:

- Export control laws, including the Export Administration Act and Regulations⁸ and other export laws where necessary.⁹ Does the program screen all transactions to prevent sales to restricted destinations? To restricted persons? Does it implement the obligations required to

prevent the use of commercial technology in weapons proliferation?¹⁰

- The Treasury embargo programs on Cuba, Iran, Iraq, Libya, North Korea, UNITA (Angola) and Yugoslavia (Serbia and Montenegro).¹¹ Are all transactions screened to prevent shipments or sales to these destinations? What about the offshore front companies and agents of these countries, the "specially designated nationals?"¹²

- The U.S. Antiboycott Law, which prohibits compliance with the Arab League economic boycott of Israel.¹³ Does the program identify reportable requests? Does it limit what can be said in response and provide an opportunity for expert input?

- The Foreign Corrupt Practices Act (FCPA), which prohibits the bribery of foreign officials.¹⁴ Does the program screen payments to foreign officials? Are accounting records maintained properly? Does the program screen agents or distributors? Does it monitor their compliance? Does it educate them on FCPA restrictions?

Is the internal program up to date? When was the last time the program was dusted off and reviewed, top to bottom? Has its scope kept pace with the company's business? How are new legal developments implemented in the program?

Managing compliance should not be confused with ensuring compliance. Putting a program in place, tinkering with it occasionally, and letting it operate is the objective in a corporate setting. Knowing how to test the program, and whether it is sufficient to reduce or eliminate the risks to the company, is the area for focus by counsel.

Managing Mistakes

The second type of compliance management in international operations is to manage mistakes. When the compliance program fails and a mistake occurs, is the company ready to manage it?

Minimize mistakes. One of the first issues in managing mistakes is to do everything possible to minimize them - which is after all the purpose of a compliance program. Allocate compliance resources to the big exposure areas.

Promote disclosure. Foster a climate that promotes self-discovery and internal disclosure. Compliance program managers and business officials should report violations to counsel, not hide them, downplay them or ignore them.

Conduct audits. Find mistakes first, before others do. Develop a good internal review system. Conduct internal audits.¹⁵ Spot-check problem or weak areas.

Jeffrey L. Snyder is a partner and chair of Crowell & Moring LLP's International Practice Group. At the time this article published Mr. Snyder was with the law firm of Graham & James.

Guard against the ostrich: Take steps to prevent the "head-in-the-sand" problem.

Prepare for inquiries. If counsel does not find the problems first, he or she should develop a strategy to handle inquiries and contacts from the government agencies that do. Enforcement agencies have a variety of techniques, from phone calls and letters to direct visits. Because they often will not contact company counsel first, counsel must prepare all managers and those who deal with the public (receptionists, guards, etc.) for approaches from investigators, auditors and government agents. Company staff must know that they should contact counsel immediately, what they can and cannot say, and other techniques to prevent mistakes in those early moments of the approach.

Voluntary self-disclosure. Finally, counsel should be aware of voluntary self-disclosure procedures for violations in this area.¹⁶ It is important to learn beforehand how they work and what voluntary disclosure means. Most of all, counsel must be prepared so as to avoid the delay that usually accompanies decisions to disclose.

Issues for the Future

Compliance problems are not fading. In fact, just the opposite is true. New laws are coming into effect, such as the new measures on trade with Iran.¹⁷ Other laws are being rewritten, such as the Export Administration Regulations.¹⁸ These and others will challenge the best of compliance managers to develop new techniques and strategies.

Among the issues of concern is the automated export system, or AES. The U.S. Customs Service is making a move to "paperless" exports, to parallel its automated import procedures. As Customs moves to automated processing of export documents, a variety of new compliance issues will arise. These issues are even more acute in an era in which general export licenses are more common and the information filed with Customs becomes the primary enforcement tool for export violations.

Customs is actively involved in the enforcement of some of these laws. Some would have Customs take on more of a role. How Customs handles enforcement activity and deals with issues such as mitigation and disclosure may soon be of greater significance.¹⁹

A successor regime to the Coordinating Committee for the Multilateral Control of Exports, or COCOM, has just come into being,²⁰ even though COCOM ceased to exist in early 1994. A new multilateral regime will mean new compliance issues as the new laws filter down into national legislation. If a new regime is not created, the use of unilateral national laws will create difficult compliance issues, particularly for multinationals who will face the different standards and rules in different countries.

Although it is standard U.S. policy to avoid unilateral controls, the United States has not been successful in obtaining a multilateral consensus on any of the four laws that are discussed here. This trend does not show any signs of changing course. It is therefore more than likely that there will be only more conflicts among national laws. Compliance programs that must address the laws of one nation are difficult enough to implement.

Finally, with the end of the Cold War, national intelligence services have turned their attention to commercial espionage.²¹ This means that companies engaged in international operations need to consider the risks for their operations and develop programs designed to reduce or eliminate them.

Conclusion

While compliance in the last half of the 1990s may be no more complicated than it was before, the changing patterns of business for companies operating internationally means new challenges. Managing compliance has never been more difficult.

In many cases, companies are not aware of legal obligations or compliance mandates until after a violation occurs. Considering compliance issues early in the process of developing international operations can assist in minimizing exposure and managing compliance efforts.



1. Lawyers practicing in the international arena face many challenges, some of which are not shared by lawyers with a purely domestic practice. Robert A. Creamer, "Lawyer Liability in International Practice," 6 Loss Prevention Journal 17, 19 (1995) (malpractice claim relating to failure to advise on necessity of export approval for technology transfer).

2. Significant penalties have been imposed under each of these laws in 1995. Even the Antiboycott Law, which is widely speculated to be on the wane due to the Middle East peace process, has resulted in the imposition of at least nine major fines this year alone, including \$1.4 million in civil penalties by L'Oreal. Lockheed paid a record \$24.8 million fine in settlement of an indictment under the FCPA.

3. See, e.g., Stephens, "International Records Retention," 29 Records Management Quarterly 69 (1995) (describing myriad recordkeeping requirements and pitfalls for international operations). Full compliance is of course a relative term and can be defined differently depending on one's position. Under any definition, however, the laws in this area are both vague and complex, each factor making full compliance impossible. The goal is to make those inevitable mistakes the small and minor ones.

4. See generally Heffelfinger, "Corporate Compliance Checklist," 19 ALI-ABA Course Materials Journal, at 85 (August 1994) (providing checklists for compliance programs in general, including reporting, auditing, investigations, training and other issues), reprinted in *Law Department Adviser*, at 9 (February 1995). A useful concept in the design and implementation of compliance programs is to "reason in reverse." Looking back from the perspective of the goal, it is often possible to see solutions in techniques that are not visible otherwise. See Dixit & Nalebuff, *Thinking Strategically* (1991).

5. See generally *Export Administration Annual Report 1994 and 1995 Report on Foreign Policy Controls*, at pp. II-39 ("A systematic review of SEDs at EE Headquarters is conducted after shipments have occurred. OES receives from the Census Bureau microfilm copies of the actual SEDs and a computerized index of data fields that includes the license symbol, ECCN and Schedule B number for every SED. OES uses the index to produce a list of SEDs for transactions that may warrant further review, focusing particularly on validated license shipments, certain general license shipments, shipments bound for destinations of concern, and shipments of strategic commodities of proliferation concern. SED searches may also be customized. ... Over the past year, OEE initiated over 500 investigations of suspected export control violations on the basis of routine reviews of SEDs.").

6. See Davidson, "Sentence Rules Mainly Snag

Small Firms," *Wall Street Journal*, Aug. 28, 1995, at B3, col. 3 (describing impact of sentencing guidelines for corporate criminal violations as falling heavily on smaller corporations).

7. See Rocchini and Olinsky, "Is Your Legal Compliance Program Merely A Paper Tiger?," *Corporate Legal Times*, at 29 (June 1994).

8. 50 U.S.C. app. 2401 et seq., 15 C.F.R. § 768 et seq.

9. Munitions exports are controlled under the Arms Export Control Act, 22 U.S.C. § 2752 et seq., and the International Traffic in Arms Regulations, 22 C.F.R. Part 120 (1995). Other items are subject to special controls, such as narcotics, atomic energy items, contain watercraft, natural gas, tobacco seeds, endangered wildlife and certain patent application information. See 15 C.F.R. § 770.10 (1994).

10. Proliferation controls were introduced in 1990 by President Bush in the Enhanced Proliferation Control Initiative, or EPCI. EPCI controls prohibit the use of a general export license if the exporter knows or has reason to know that the exported item will be directly employed in a proliferation activity. 15 C.F.R. § 778 (1994). The EPCI proliferation controls present special problems from a compliance program perspective because they require that exporters exercise judgment and common sense, which can weaken a compliance program.

11. The Treasury Department's Office of Foreign Assets Control maintains its various embargo programs under the authority of the Trading With the Enemy Act, 50 U.S.C. app. 5(b), § 16, and the International Emergency Economic Powers Act, 50 U.S.C. § 1701-06. The statutory provisions are very general; each of the programs is implemented in detailed regulations in 31 C.F.R. Part 500 ff.

12. The list of specially designated nationals is now published by the Commerce Department as part of the Export Administration Regulations, 15 C.F.R. § 788 (1994).

13. The Antiboycott Law is found in § 8 of the Export Administration Act, with detailed regulations at 15 C.F.R. § 769, part of the Export Administration Regulations.

14. 15 U.S.C. § 78m(b)(2), (3); 78 dd-1, 2; 78ff(a), (c).

15. See *Corporate Counsel's Guide to Legal Audits & Investigations* (1995).

16. See, e.g., 15 C.F.R. § 787.15 (1994) (Voluntary Self-Disclosure Program for Export Control Violations). See generally Bialos, "The Detection and Disclosure of Violations of U.S. Export Controls: Management Choices and Their Security Implications," 29 Va. J. Int'l L. 567 (1989).

17. Iranian Transaction Regulations; Implementation of Executive Orders 12957 and 12959, 60 Fed. Reg. 47061 (Sept. 11, 1995).

18. Simplification of Export Administration Regulations: Proposed Rule, 60 Fed. Reg. 25267 (May 11, 1995).

19. Baker, "Shifts in Direction Planned for Customs Enforcement," *Corporate Counsel's International Adviser*, Sept. 1, 1995, at 124-02; "U.S. Customs Enforcement at a Glance," *The Export Practitioner*, July 31, 1995, at 13.

20. "Work Continues on New Regime of Export Controls," *BNA International Trade Reporter*, Sept. 20, 1995, at 1556.

21. See *Annual White House Report to Congress on Foreign Economic Collection and Industrial Espionage 1995* (describing specific activities and techniques).