



Export Controls, Economic and Trade Sanctions: The Challenges and Risks

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Introduction



▪ Agenda

- ▶ Overview of export control regimes
 - International Traffic in Arms Regulations
 - Export Administration Regulations
- ▶ Export control reform: status and what to expect
- ▶ U.S. sanctions programs
- ▶ Identifying, understanding, and minimizing risks

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Landscape



- **Well-trained engineers, capital, and technology no longer concentrated in one country or region;**
- **Export controls and regulations are complex and can change with little notice or warning;**
- **Violations are punished by fines, temporary/permanent export bans, imprisonment of senior executives, and can lead to negative publicity;**
- **Companies need to evolve their own practices to fit their unique organizational structure and business practices.**

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Primary Players



- **Department of Commerce**
 - Commercial/dual-use goods, technology and software
- **Department of State**
 - Military hardware, technology, software
 - Defense services
- **Mutually-exclusive jurisdiction**
- **Commodity jurisdiction requests to State**
- **Department of Treasury**
 - Economic and trade sanctions programs

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Export Control Under the EAR



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Commercial / Dual-Use Items



- **Department of Commerce**
 - Bureau of Industry & Security (“BIS”)
 - Export Administration Regulations (“EAR”)
 - Commerce Control List (“CCL”)
- **Controls the export and reexports of “dual use” and commercial products.**
 - “Dual-Use” is a term used to distinguish items controlled by the EAR from those controlled by other agencies.
 - Dual-Use products can be used in military applications AND in commercial applications.

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EAR



- **Implement the Export Administration Act through the International Economic Emergency Powers Act**
- **Contained in 15 CFR Parts 730-774**
- **Applies to virtually all goods in the United States or U.S.-origin**



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Activities Controlled Under the EAR



- **Transfer/movement from the US to foreign destination**
 - By any method
 - Even temporarily
- **Transfers of technology or source code within the US**
- **Release abroad of technology or software**
- **Reexports of US-origin items**
- **Exports of certain foreign-made items**

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Basic Concepts Under the EAR



- **Most exports and reexports will not require a license**
- **Nevertheless, exports to some destinations or end-users will need a license (know “what,” “where,” “who,” and “what use”)**
- **“Red flags” indicating abnormal circumstances**

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The Commerce Control List



- **Items are classified under specific Export Control Classification Numbers (“ECCNs”) within one of ten specific categories on the Commerce Control List.**
- **The CCL categories include:**
 - 0: Nuclear materials, facilities and equipment (and miscellaneous items)
 - 1: Materials, chemicals, microorganisms, and toxins
 - 2: Materials processing
 - 3: Electronics
 - 4: Computers
 - 5: Telecommunications and information security
 - 6: Sensors and lasers
 - 7: Navigation and avionics
 - 8: Marine
 - 9: Propulsion systems, space vehicles, and related equipment

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The Commerce Control List



- **Each of these categories is further divided into five product groups, including: (A) systems, equipment and components, (B) test, inspection and production equipment, (C) material, (D) software, and (E) technology.**
- **Items that are not specifically identified on the CCL are classified as “EAR99.”**

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Encryption Controls



- **Determining obligations under EAR controls for products designed to use encryption**
 - Classification
 - Review and Reporting Requirements

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Export Control Under the ITAR

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Military Items



- **Department of State**

- ▶ Directorate of Defense Trade Controls (“DDTC”)
- ▶ International Traffic in Arms Regulations (“ITAR”)
- ▶ US Munitions List (“USML”)

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The ITAR



- **The ITAR implements the Arms Export Control Act**
- **22 C.F.R. Parts 120-130**
- **Key Elements**
 - ▶ U.S. Munitions List
 - ▶ Significant Military Equipment
 - ▶ Prohibited Countries
 - ▶ Congressional Notification

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Basic Concepts Under the ITAR



- **Most exports and re-exports will require a license**
- **If an item is on the USML, its export will require a State Department license or other authorization unless an exemption applies**
- **Manufacturers and exporters must register and notify DDTC of certain changes**

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What is Controlled Under the ITAR?



- **Defense Articles:**
 - Hardware
 - Technical data/software (not technical data in the public domain)
 - Even if technology was developed for a commercial use, if it is modified for a military purpose it will become ITAR-controlled
 - Defense services

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Deemed Exports



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Technology and “Deemed Exports”



▪ Definition

- ▶ Release of technology or source code to a foreign national, *even if within the US*
- ▶ Deemed to be an export to the foreign national’s home country

▪ Exceptions

- ▶ Permanent residents
- ▶ Protected individuals

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Technology and “Deemed Exports”



▪ How do releases of technology occur?

- ▶ Visual inspection by foreign nationals of US-origin equipment and facilities
- ▶ Oral exchanges of information in the US or abroad
- ▶ Information exchange through emails, mail, faxes, plant visits and video conferences
- ▶ Accessing information from US or abroad of US-based databases
- ▶ Application to situations abroad of personal knowledge or technical experience acquired in the US

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Export Control Reform



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Export Control Reform



- **Export control reform – the horizon and beyond**
 - ▶ 3 Phases
 - ▶ Current Status
- **Satellite jurisdiction – NDAA §1261 and the rewrite of USML Category XV**
- **Brokering – status of proposed rule**

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Sanctions



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Outline



- **I. Basic Background**
- **II. Issue-Spotting**
- **III. Specially Designated Nationals**
- **III. Iran**
 - Overview of Program
 - 2012 / 2013 Changes
- **IV. Syria**
 - Overview of Program
 - 2012 Changes
- **V. How Quickly It Can Change – Burma**
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I. Basic Background: Overview



- **Foreign Policy Tool – Complementing Export Controls**
 - › Controls on Export based on product (*e.g.*, EAR/ITAR)
 - › Controls on Export based on end-user (*e.g.*, SDN List)
 - › Controls on Export based on destination (*e.g.*, Sanctions)
- **Types of Sanctions**
 - › Asset Freeze / Blocking of Property
 - › Service Prohibition
 - › Currency / Foreign Exchange Prohibition
- **Administered by the U.S. Treasury Department**
 - › Office of Foreign Assets Control (“OFAC”)

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I. Basic Background: List of Programs



- **Full Embargoes**
 - Cuba, Iran, North Korea, Sudan, Syria
- **Other Country Specific Programs**
 - Balkans, Belarus, Burma, Cote D'Ivoire, Congo, Iraq, Liberia, Libya, Lebanon, Somalia, and Zimbabwe
- **Issue-based programs**
 - WMD; Non-proliferation; Terrorism; Counter-narcotics; Diamond Trading (Kimberley); and Transnational Crime

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I. Basic Background: Statutory Authority



- **International Emergency Economic Powers Act (IEEPA)**
 - › 50 U.S.C. 1701 *et seq*
 - › Presidential authority for “any unusual and extraordinary threat, which has its source in whole or substantial part outside the United States, to the national security, foreign policy, or economy or the United States, if the President declares a national emergency with respect to such threat”
- **United Nations Participation Act (UNPA)**
 - › Implement UN Security Council resolutions through sanctions
 - › Can’t go beyond the mandate in the UNSC Resolution
- **Trading With The Enemy Act (TWEA)**

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I. Basic Background: Jurisdiction



▪ **U.S. Person**

- ▶ “The term “United States Person” means any United States citizen, permanent resident alien, entity organized under the laws of the United States or any jurisdiction within the United States (including foreign branches), or any person in the United States.”
- ▶ Generally, not foreign Subsidiaries of U.S. companies
 - EXCEPT with respect to Cuba and now Iran

▪ **U.S.- Origin Goods**

- ▶ Items produced in the United States
- ▶ Foreign items incorporating more than de minimis U.S. content
- ▶ Items which transit the United States

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I. Basic Background: Penalties



▪ **Civil Penalties**

- ▶ Greater of \$250,000 per violation OR twice the transaction value
- ▶ *e.g.*, JP Morgan - \$88,300,000 in August 2011 for alleged violations of Cuba, Iran, Sudan, Liberia, WMD and Terrorism Sanctions programs

▪ **Criminal Penalties**

- ▶ “Willfully commits, willfully attempts to commit, or willfully conspires to commit ...”
- ▶ \$1,000,000 per violation;
- ▶ 20 year maximum prison sentence
- ▶ Export denial

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II. Issue Spotting



▪ **These programs change quickly and vary dramatically**

- ▶ By sanctioning country (e.g., variance between U.S. and EU)
- ▶ By sanctioned country (e.g., different restrictions on Iran & Syria)
- ▶ Over time (e.g., substantial revisions over 2012)

▪ **Identifying if jurisdiction exists**

- ▶ Increasing assertion of U.S. jurisdiction over non-U.S. persons
- ▶ Transshipment of products
- ▶ “Deemed exports” to foreign persons in the United States

▪ **Major potential liability in M&A transactions**

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III. Specially Designated Nationals (SDNs)



- **Individuals can be “designated” by OFAC under sanctions regimes**
- **Designations result in a variety of punishments:**
 - › Freezing/blocking of assets
 - › Prohibition on U.S. government contraction
- **U.S. Persons are prohibited from transacting with SDNs**
 - › End-user, freight forwarder, consignee, etc
- **Compliance Steps**
 - › Always screen every party to a transaction
 - › Designations change so must continually monitor
 - › Consolidated Screening List available at
 - http://export.gov/ecr/eg_main_023148.asp

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IV. Iran



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III. Iran: Restrictions on U.S. Persons



- **Full Embargo**
 - › Import Ban on Goods and Services of Iranian Origin
 - › Export /Reexport Ban on U.S.-Origin Goods, Tech., or Services
 - › New Investment Prohibition in Iran
- **Exceptions**
 - › Iranian nationals resident in U.S. can provide services
 - › Travel and incidental transactions are authorized
 - › Informational Materials
 - › Foreign subsidiaries (if no U.S. person approval/facilitation)

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III. Iran: Restrictions on All Persons



Iran Sanctions Act of 1996

- › Congress targeted Non-U.S. persons in Iran's Refined Petroleum Sector
- › Investments of \$20 million or more in Iran's ability to develop refined petroleum
- › Provided goods/services/tech. to assist Iran with its refined petroleum production
- › Mandatory imposition of sanctions included prohibitions on:
 - Ex-Im financing; export licensing; loans from U.S. financial institutions; and access to U.S. government contracts

Comprehensive Iran Sanctions and Divestment Act of 2010

- › Expanded Iran Sanctions Act to cover additional activities
 - Development of Petroleum Resources in Iran
 - Lowering threshold from \$20 to \$5m investment in refined petroleum
 - Export of refined petroleum to Iran
 - Transfer of nuclear technology to Iran
- › Added additional sanctions
 - Access to foreign exchange, access to U.S. banking sector, etc
 - Government contractor certification of compliance

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III. Iran: Changes in 2012/2013



2012 National Defense Authorization Act (Sec. 1245)

- **Targeted Iranian financial sector**
 - › Designated the entire Iranian banking sector as a jurisdiction of "primary money laundering concern"
 - › Froze assets of all Iranian banks in the United States
- **Restrictions on Foreign Financial Institutions**
 - › No pay-through or correspondent accounts in the U.S. for Iranian end users
 - › Cannot facilitate purchase of petroleum or petroleum products from Iran
 - Even if no U.S. nexus

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III. Iran: Changes in 2012/2013



H.R. 1905 – Iran Threat Reduction and Syria Human Rights Act

- **Expanded ISA/CISADA to cover "Petrochemical Products" (Sec. 201)**
- **Prohibit importation of Iranian crude oil (Sec. 202)**
 - › Unless a waiver issued every 6 months by the President
- **Expanded ISA sanctions**
 - › Sanctions on individual executive officers
- **Liability of Parents or actions of non-U.S. subs/affiliates (Sec. 218)**
 - › Knowingly undertook action U.S. person could not take
- **Imposition of mandatory SEC reporting obligation (Sec. 219)**
 - › All issuers (including foreign entities) required to file quarterly/annual reports
 - › Must now report
 - Knowing violations of ISA/CISADA
 - Knowing interactions wit SDNs
 - Reports trigger automatic investigation

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III. Iran: Changes in 2012/2013



2013 - National Defense Authorization Act

- **Additional Designations**
 - › All port operators and
 - › All entities in the energy, shipping and shipbuilding sectors
- **Expanded ISA/CISADA to include *inter alia***
 - › Goods or services used in connection with energy, shipping or shipbuilding sectors (Sec. 1244)
 - › Precious metals (Sec. 1245)
 - › Graphite, aluminum, steel, and coal (Sec 1245)
 - › Individuals supplying insurance or reinsurance to SDNs (Sec. 1246)
 - › Foreign financial institutions facilitating transactions w/ SDNs (Sec. 1247)

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III. Iran: Government Contractor Specific Risks



- **FAR 25.703 – Prohibition on Contracting with Entities that Engage in Certain Activities Relating to Iran**
 - › Implements ISA and CISADA restrictions
- **Certification Required for acquisition of products / services**
 - › FAR 52.25-1103(e) – Include certification required in “each solicitation for the acquisition of products or services.”
 - › **FAR 52.225-25 – Prohibition on Contracting with Entities Engaging in Sanctioned Activities Relating to Iran**
 - › Offeror does not export sensitive technology to Iran
 - › Does not engage in activities sanctioned by ISA/CISADA

**Bold = 2012 Changes

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IV. Syria



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IV. Syria: Overview of U.S. Program



- **Pre-Existing Prohibitions**
 - › Export ban for U.S.-origin goods or technology under the Export Administration Regulations (EAR) & International Traffic in Arms Regulations (ITAR)
 - › Blocking sanctions on certain designated Syrian nationals
- **2012 Expansion of Sanctions**
 - › ****Blocking Syrian Government Property**
 - › ****Prohibiting new investment in Syria by U.S. persons**
 - › ****Prohibition the provision of services to Syria by U.S. persons**
 - › ****Prohibiting the import of petroleum or petroleum resources**
- **Exceptions**
 - › Travel
 - › Transactions incident to residence in Syria
 - › Export of export of food and medicine
 - › Services incident to export of licensed U.S.-origin products
 - › Diplomatic missions and International Governmental Institutions

**Bold = 2012 Changes

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IV. Syria: Overview of EU Sanctions



- **Prohibition on the sale, supply, transfer or export of:**
 - › Arms
 - › Gold, precious metals and diamonds,
 - › Luxury goods
 - › Specified "Dual-use" items that could be used for internal repression
 - › Hardware or software for monitoring or intercepting communications
 - › Technology or equipment for the natural gas or oil sector
 - › Prohibition on providing technical, financial or brokering services related to the above
- **Targeted sanctions on certain individuals**
 - › Asset Freeze
 - › Travel ban
- **Miscellaneous Additional Sanctions**
 - › Prohibition on participation in the construction of power plants
 - › Prohibition on Syrian banks opening new branches or subsidiaries in the EU and EU banks from doing the same in Syria

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V. How Quickly It Can Change: Burma



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V. How Quickly It Can Change: Burma



Timeline for Winding Down Sanctions

- Nov. 18, 2011 – Secretary of State Clinton travels to Burma
- April 17, 2012 – U.S. Normalizes Relations with Burma
 - OFAC Authorizes certain financial services in support of humanitarian or non-profit activities (GL 14-C)
- April 23, 2012 – EU suspends sanctions (except arms embargo)
- July 11, 2012 – OFAC Authorizes:
 - Export / reexport of all financial services to non blocked parties (GL 16)
 - New investment in Burma provided a reporting requirement is met (GL 17)
- Sept. 26, 2012:
 - Sec. Clinton commits to suspending import ban
 - FinCen withdraws money laundering designations on two Burmese banks
- Oct. 18, 2012 – U.S. authorizes International Financial Institution Investment

Sanctions still in place

- U.S. and EU Maintain a blocking regime on military and former key leaders
- Import ban remains in place

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VI. Conclusion



- **Constantly Changing Environment**
 - › Compliance and sales teams need to continually monitor changes
- **Key Initial Questions To Ask**
 - › (1) Does a transaction involve a sanctioned country
 - › (2) Does it involve a U.S. person, product or potential jurisdiction
 - (Even foreign subsidiaries in transactions with Iran or Cuba)
 - › (3) Has a License Been Issued?
- **If the answers are yes or unclear, reach out to your experts**

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Evaluating Risk



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Strategies for Risk Management



- **Awareness and compliance focus**
- **Understanding and effective use of rules and exemptions**
 - STAY CURRENT!
 - Sanction Regimes Change Quickly
- **Tools & resources for robust compliance program**

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General Export



- **Do you maintain export compliance policies? How regularly are these policies updated?**
- **Do you have designated personnel for export compliance?**
- **Do you conduct training for export compliance? How regularly?**
- **Do you have a recordkeeping system for export compliance?**
- **Do you conduct internal audits/reviews of compliance? How regularly?**

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Foreign Nationals



- **Do you maintain a specific HR policy addressing export control issues arising from the employment or assignment of foreign persons to work at your facility?**
- **Do you have procedures in place to ensure authorization exists for the transfer of any controlled technology?**
- **Do you maintain processes for accessing the company's computers or databases?**
- **Do you have a process for managing export control risks from foreign travel?**
- **Do you have procedures for visits by foreign nationals to your facilities?**

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Commodity Classification



- Do you have any products or technology classified on the Commerce Control List?
- Have you obtained any formal Commerce Commodity classifications?
- Do you have any products controlled under the US Munitions List?
- Have you submitted any Commodity Jurisdiction requests?

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Sanctions



- Do you screen existing customers for eligibility to receive US-origin goods, services, or technologies?
 - If so, when?
- Do you screen for destinations subject to sanction or embargo?
 - Do you conduct business in Iran, North Korea, Sudan, Syria or Cuba?
- Do you screen for red flags or diversion risk assessment?

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Conclusion



Questions?

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