

## Recent Developments in U.S. Trade Controls

Presentation to the Society of Corporate Compliance and Ethics  
September 28, 2016

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### Agenda

- Sanctions developments
  - Iran
  - Cuba
  - Russia and Crimea
  - Miscellaneous
- Export control reform
  - Impact of export control reform during Obama Administration
  - Recent developments in cloud/cyber
  - What to expect from the next Administration
- Enforcement
  - Key trends, including individual liability risk
  - Recent case on "reason to know"
- Brexit

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2

### U.S. Trade Controls: Recap of Key Programs

- Dual-Use Goods and Technology: Export Administration Regulations ("EAR") administered by the Department of Commerce, Bureau of Industry and Security ("BIS")
- Defense Articles and Defense Services: International Traffic in Arms Regulations ("ITAR") administered by the Department of State, Directorate of Defense Trade Controls ("DDTC")
- Economic Sanctions: Various regulations administered by the Department of the Treasury, Office of Foreign Assets Control ("OFAC")
- Antiboycott Measures: Two different regimes enforced by the Commerce Department through the EAR and the Treasury Department through the tax code

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3

## Iran Sanctions: Overview

- Comprehensive "primary" sanctions imposed in 1990s
  - Response to U.S. concerns over Iran's support for terrorism and pursuit of WMD
  - Expanded in October 2012 to reach the Iran-related activities of non-U.S. companies owned or controlled by U.S. persons
- Significant expansion of "secondary" or "retaliatory" sanctions from 2010-2013 in response to concerns regarding Iran's nuclear program
  - Secondary sanctions can be imposed against non-U.S. entities engaged in certain "sanctionable" Iran-related conduct
- As a result of sanctions relief, some secondary sanctions lifted, but not all; primary sanctions remain in place

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## Iran: Easing of Primary Sanctions

- Primary sanctions that prohibit U.S. persons and their owned or controlled non-U.S. affiliates from engaging in virtually any Iran-related dealings largely remain in place.
- Several aspects of primary sanctions were eased in 2016, in part through the new General License H, which authorizes:
  - Non-U.S. entities owned or controlled by a U.S. person to engage in Iran-related dealings, subject to certain conditions
  - Limited facilitation by U.S. persons authorized
    - Initial determination as to whether owned or controlled U.S. subsidiary will engage in Iran-related dealings
    - Establishment or alteration of operating policies and procedures of a U.S. entity or an owned or controlled non-U.S. subsidiary, to the extent necessary to allow the non-U.S. subsidiary to engage in permissible Iran-related dealings
    - U.S. parent companies may make available to their owned or controlled non-U.S. subsidiaries automated and globally integrated business support systems

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## Iran: Easing of Secondary Sanctions

- Ceased application of "nuclear-related" secondary sanctions
- Significant impact on non-U.S. companies not owned or controlled by a U.S. person that seek to do Iran-related business in the following sectors:
  - Energy
  - Shipping and Shipbuilding
  - Automotive
  - Financial services and insurance
  - Metals and industrial process software
- Relief does not extend to secondary sanctions imposed in connection with Iran's support for terrorism, human rights abuses, or weapons proliferation and missile activities



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**Iran: Continuing Secondary Sanctions**

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- Secondary sanctions continue to apply to non-U.S. persons that, among other things, knowingly:
  - Provide support for an activity or transaction on behalf of or for the benefit of an Iranian SDN
  - Sell, supply, or transfer to or from Iran significant goods or services used in connection with the energy, shipping, or shipbuilding sectors if the transactions involve an SDN
  - Provide support for, or engage in a significant transaction with, the IRGC or its blocked officials, agents, or affiliates
  - Sell, supply, or transfer to or from Iran certain metals and software if the transaction involves an SDN or nuclear, military, or ballistic missile end use
  - Provide goods or technology likely to be used to commit serious human rights abuses

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**Iran: Possibility of “Snap Back”**

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- OFAC authorization applies only to activities conducted during the period of sanctions relief
- If sanctions “snap back” because Iran has failed to adhere to the JCPOA, contracts entered into during the period of sanctions relief would not be grandfathered
  - Secondary sanctions could be applied
- Any activity conducted after the snapback could be subject to the reimposed primary sanctions
- OFAC has provided general assurances that the U.S. will seek to minimize the effects of a potential snapback without making any specific commitment of flexibility

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**Cuba: Overview**

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- U.S. embargo of Cuba dates back a half century
  - Broad ban on export/import trade in goods and services, and exports/reexports of U.S.-regulated goods/technology
  - Applies to U.S. persons and owned or controlled U.S. affiliates
- Recently there has been a gradual thawing of U.S.-Cuba relations
  - U.S. embassy in Havana was reopened
  - President Obama visited in March 2016
  - Cuba was removed from “State Sponsors of Terrorism” list
- Certain aspects of the embargo have been eased in the past year and a half
- But, key elements of the embargo remain -- and Congress would have to act to lift them

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**Cuba: Recent Developments**



- Restrictions eased with respect to:
  - Certain types of trade:
    - Trade with the Cuban private sector or benefitting the Cuban people
    - Trade in telecommunications items
    - Exports related to commercial aviation
  - Travel to Cuba for particular purposes (not tourist travel)
  - Financial services
  - Remittances



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**Cuba: Recent Developments**



- Examples of trade now permitted:
  - U.S. companies can establish a "physical presence" in Cuba related to authorized activities – in other words, open an office, store, or warehouse
  - Expanded travel authorized, including for purposes of professional meetings and professional research
  - Broad informational exchanges (media, sports, music, etc.)
  - Licensing available for exports related to public infrastructure, water treatment, and other projects that help the Cuban people

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**Cuba: Sanctions Still In Place**



- No unlicensed export/import trade with Cuba worldwide by persons subject to U.S. jurisdiction, unless authorized
- No investment in Cuba, unless authorized
- No dealings with entities owned or controlled by Cuba, unless authorized
- No dealings in Cuban property, unless authorized
  - Includes asset-blocking requirement. Generally, property in which Cuba or a Cuban national has an interest that comes within the United States or the possession or control of a U.S. person must be "blocked" (frozen)
  - Extends even to property in which a blocked Cuban party has a minority interest

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**Russia and Crimea: Overview**

- Russia is not subject to a broad embargo, but the Crimea region of Ukraine is subject to a broad embargo
- The United States also has imposed targeted and “sectoral” sanctions on certain individuals and entities involved in the crisis in Ukraine
- 3 key U.S. lists for purposes of Ukraine/Russia sanctions:
  - OFAC SDN List
  - OFAC Sectoral Sanctions Identifications List (“SSI List”)
  - Commerce/BIS Entity List
- Commerce/BIS has imposed additional restrictions:
  - Certain products for energy sector
  - Certain products for military end-use or end-users

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**Crimea Sanctions**

- U.S. has targeted the Crimea region of Ukraine, which Russia purported to annex, prohibiting:
  - “New investment” in the Crimea region
  - Importation into the United States, directly or indirectly, of any goods, services, or technology from the Crimea region
  - Exportation, reexportation, sale, or supply, directly or indirectly, of any goods, services, or technology to the Crimea region
  - Any approval, financing, facilitation, or guarantee of a transaction by a foreign person that would be prohibited if performed by a U.S. person or within the United States

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**Russia: OFAC SSI List**

- Directives 1-3 prohibit transactions in, provision of financing for, and other dealings in:
  - New debt of SSI List entities:
    - >30 days maturity for listed financial institutions and defense companies
    - >90 days maturity for listed energy companies
  - New equity of SSI List financial institutions
- Directive 4 prohibits providing, exporting, or reexporting, directly or indirectly, goods, services, or technology in support of:
  - Exploration or production from deepwater (>500 ft), Arctic offshore, or shale projects that:
    - Have the potential to produce oil in or offshore Russia; and
    - Involve energy companies listed in Directive 4 or those entities they own (50% or more)

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## North Korea

- In March 2016, a new Executive Order:
  - blocked all property of the North Korean Government or Workers' Party of Korea
  - prohibited the exportation or reexportation from the United States or by a U.S. person of any goods, services (including financial services), or technology to North Korea
  - prohibited all new investment in North Korea by any U.S. person
  - banned any financing or facilitation of transactions that would be prohibited if performed by a U.S. person or within the United States.
- On July 6, OFAC added Kim Jong Un to the List of Specially Designated Nationals and Blocked Persons ("SDN List") for his ties to human rights abuses
- OFAC designated ten other high-ranking individuals and five ministries and departments within the North Korean regime for human rights abuses.

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## Burma

- On May 18, OFAC took additional steps to ease certain economic sanctions on Burma (Myanmar), recognizing Burma's recent progress in implementing democratic reforms. Specifically, OFAC:
  - Established and expanded general licenses for banking services, personal transactions for U.S. persons in Burma, and trade-related transactions
  - Removed seven state-owned enterprises and three state-owned banks from the SDN List
- OFAC also added an additional six entities to the SDN List in an effort to further incentivize continued democratic reforms in Burma.
  - All six companies are owned 50 percent or more by Steven Law or Asia World Co. Ltd., which are already designated on the SDN List.
  - According to OFAC, those Burmese individuals and entities that currently remain subject to U.S. sanctions have been targeted due to obstruction of political reform, human rights abuses, or propagation of military trade with North Korea.

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17

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## Developments in Export Controls

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### Export Control Reform: Background

- In August 2009, President Obama pledged to "reform export controls consistent with national security"
  - Higher fences around fewer items
  - Possible consolidation of agencies and functions
  - Some administrative reforms, some by legislation
  - Intended to improve interoperability with allies, strengthen the U.S. industrial base, and ease licensing burden on U.S. exporters
- The Administration launched the Export Control Reform Initiative ("ECR Initiative") in response

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### Export Control Reform

- ECR Initiative is being implemented in three phases:
  - Phase I & Phase II: Revise the USML and reconcile various ITAR/EAR definitions and policies, building toward Phase III
  - Phase III: Creation of a single control list, single licensing agency, unified information technology system, and enforcement coordination center
- Phase I is finished and Phase II is nearly complete. Many of the USML categories have been revised, with corresponding movement of items to the CCL ("600-series" and "500-series" ECCNs)
- For Phase III, an export enforcement coordination center has been created and agencies are working toward a unified licensing platform
  - But not close to a single control list or single licensing agency

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### Recent Revisions to Cloud and Encryption Regulations

- BIS issued amendments to the EAR on June 3, 2016
  - **Physical Access to Hardware:** Physical access to hardware does not constitute a "release" of technical data unless such data are revealed or accessed thereby.
  - **Encrypted Data:** Sending, taking, or storing EAR-controlled technology or software is not an export, reexport, or transfer if:
    - Unclassified
    - Secured using "end-to-end encryption"
    - Encryption meets certain NIST standards or equivalent
    - Technology or software is not "intentionally" stored in a country in Country Group D:5 (including China, Iraq, or Vietnam) or Russia
- Effective date is September 1, 2016

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**Recent Revisions to Cloud and Encryption Regulations**

- DDTC issued a companion rule on June 3, 2016
  - Did not include changes related to treatment of encrypted ITAR-controlled technical data and software
  - Did not include changes to defense services rule
  - Liberalized an exemption related to exports of and access to ITAR-controlled technical data by both U.S. persons and foreign person employees of a U.S. company, when traveling or on temporary assignment abroad (subject to certain restrictions)
- Effective date is September 1, 2016

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**Revised BIS Guidance on Export Control Settlements**

- On June 22, BIS issued a final rule revising BIS's guidance on charging and penalty determinations when settling administrative export control enforcement cases
- Rule took effect on July 22
- BIS adopts the State / DDTC practice of permitting, in some cases, the suspension of civil penalties to allow offenders to use the funds for compliance activities required under the final order, such as improving internal compliance programs and conducting audits.
- BIS continues its past emphasis on the importance of voluntary self disclosures (VSDs):
  - assigns "great weight" to VSDs as a mitigating factor
  - expressly contemplates a 50% reduction in base penalties for violations properly and completely disclosed by VSD

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23

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**Enforcement**

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### Enforcement: Summary

- Trends: aggressive enforcement, increasing cooperation among agencies (E2C2) and with DOJ
- Potential for high penalties, other severe consequences (debarment, denial of export privileges)
- Targeting of individuals, not just companies
- Enforcement targets: illegal trade with China and with sanctioned countries (especially Iran); activities related to terrorism and weapons proliferation

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### Increased Civil Penalties

- All three trade control agencies increased their maximum civil money penalties (CMPs) based on an inflation adjustment required by statute.
  - DDTC more than doubled the maximum CMP from \$500,000 to \$1,094,010 per violation. Note: maximum criminal fine is \$1,000,000 per violation - see 22 U.S.C. 2778(c)
  - BIS and OFAC increased the maximum CMP from \$250,000 to \$284,582 per violation, or twice the value of the transaction, whichever is greater.
  - The maximum civil penalty for violations of the Cuba sanctions will increase from \$50,000 to \$83,864 per violation (TWEA vs. IEEPA)

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### Risk of Individual Liability

- DOJ's internal "Yates Memo" from September 2015 announced 6 measures to increase accountability from individual corporate executives
  - To qualify for any "cooperation credit," corporations must provide DOJ with all relevant facts relating to the individuals responsible
  - Criminal and civil corporate investigations should focus on individuals from the outset of an investigation
  - Criminal and civil lawyers handling corporate investigations should be in routine communication with one another
  - Absent "extraordinary circumstances," DOJ should not release individuals from civil or criminal liability when resolving a matter against a corporation
  - Corporate cases should not be resolved without a clear plan to resolve related individual cases; declinations should be personally approved by the relevant U.S. Attorney or AAG
  - Civil lawyers should focus on individuals as well as corporations, and should not consider a defendant's ability to pay in deciding whether or not to bring suit

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**Recent Case: Epsilon v. OFAC**

- Epsilon Electronics exported more than \$3.4 million in goods to Asra International Corporation in Dubai
- OFAC issued a penalty of \$4 million, based on its determination that Epsilon had reason to know Asra would resell those goods in Iran
- Epsilon sued OFAC in D.C. District Court challenging the penalty, in part based on the "inventory exception" in OFAC's Iran regs
- D.D.C. upheld OFAC's penalty decision, reasoning that there was ample indication from Asra's website to show that Asra was reselling predominantly to Iran
- **Bottom line:** Companies have "reason to know" information readily available to them, such as on their customers' websites.



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**Brexit**

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**Brexit: Dual Use and Military Trade Controls**

- Dual-use regime
  - Likely will not be significantly impacted, as EU dual use controls derive from international arrangements (e.g. Wassenaar) that the UK will remain or become a member of
  - EU will have to add the UK to the terms of its general license for the export of dual-use goods to close allies; UK will have to do the same for the EU – but this is more of a formality
- UK military trade controls are already a function of UK national law

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### Brexit: Sanctions

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- Many EU sanctions programs are unilateral and not driven by broader international commitments
- UK will need to decide whether it wishes to maintain, for instance, the EU sanctions regime against Russia, and implement those sanctions under national legislation
- Sanctions policy implications of Brexit are complex and it is too early to understand what will occur
  - Brexit might hasten the easing of Russia sanctions as Brussels works to keep the remaining EU Member States aligned and avoid further internal policy conflict
  - On the other hand, the UK might be inclined to more closely align itself with the U.S. and its more aggressive position on certain sanctions issues

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### Questions?

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