

# Lombardo Law<sup>PC</sup>

NCMA San Diego Chapter  
International Trade Update: Export Controls & FCPA

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## Overview

- Introduction: why are we here?
  - Export Control Reform (ECR)
    - Four singles
    - Where we stand today...
    - Where are we headed?
- Latest Enforcement Cases
- Sanctions / Embargoes
  - Cuba
  - Iran
  - Others?
- Foreign Corrupt Practices Act (FCPA) Update



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# Why Are We Here?

- The United States Government regulates export of defense products and technology
- DFARS 252.225-7048 requires contractors and subcontractors to have effective export compliance programs
  - Export compliance is a contractual obligation
  - DFARS 204.73 – Safeguarding Covered Defense Information (Cyber)
- Which rules apply? State, Commerce, Treasury, DoD? Or all of them?
- Large fines/penalties for violations



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# Export Controls Generally

- The U.S. Government controls exports on a case-by-case basis, in terms of:
  - Product – what?
  - Destination – where?
  - End-user – who?
  - End-use – how/why?
- When a company decides to export, it must apply these factors against each transaction
- “But we don’t export anything!”
  - Manufacturer?
  - Deemed exports?
    - Releasing/transferring (no longer potential “access”) information regarding products and technologies are “deemed exports” to foreign nationals



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# Primary Export Control Regimes



- ITAR: Administered by DDTTC
  - Applicable to all manufacturers, brokers and/or exporters of defense articles and defense services



- EAR: Administered by BIS
  - Applicable to all exporters of “dual-use” (*i.e.*, commercial) articles and services



- Sanction and embargo regulations: Administered by OFAC
  - Covers sanction programs for Cuba, Iran, Sudan, and Syria, among others



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# Export Control Reform

- In 2009, Obama begins “fundamental reform” of U.S. export controls.
  - 4 Singles: Combined List, Enforcement Agency, IT, and Licensing Agency
- From 2009 to 2016
  - Rewrote USML Categories IV through XXI
    - Removed “specifically designed” and created new “specially designed” definition
    - Created the “600-series” and new Strategic Trade Authorization (STA) exception
  - Updated other definitions: export, fundamental research, *etc.*
  - Consolidated screening list



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## Export Control Reform: Update

- May 2018: Proposed re-write of USML Categories I, II and III
- Government continues to review and update export controls
  - Notices of Inquiry (NOI) for explosives, personal protective equipment and intelligence electronics
    - USML Categories V, X, and XI
      - Fix gaps, overcontrol and/or vague wording
  - Commerce further streamlines encryption controls
- Increased penalties for export violations based on inflation
- DDTC
  - 55% reduction in licenses since export control reform
  - Redesigned website
  - Staff shortages / Vacancy rate



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## Export Control Reform: What's (could be) Next?

- Defense Export Control and Compliance System (DECCS)
  - New electronic forms: DS-7787, 7788, 7789
- Artificial intelligence controls
  - Self driving cars to autonomous weapons
- Remaining definitions: defense services, technical data, and exceptions/exemptions
- Ease export controls on guns: Final rules for USML Categories I, II, III
- Wholesale revision of the ITAR
- Export Control Reform Act of 2018 (HR 5040)
  - Focus on dual-use controls, emerging technologies and China
- Multi-lateral harmonization



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## Enforcement Trends: ZTE Case

- ZTE is telecommunications company in China: smart phones, telecommunications networks, etc
  - ~\$17B in annual sales
  - Many international subsidiaries/affiliates in other countries, including Australia, Brazil, India, etc
- Allegations:
  - From 2010 to 2016, ZTE conspired to violate U.S. trade controls by illegally shipping U.S. origin products to Iran and North Korea
    - ZTE sought to set-up a telecommunications network in Iran using U.S. origin equipment/software
    - ZTE concealed actions by using intermediary shippers, omitting references to Iran, omitting references to U.S.-origin items from packing lists (or commingling U.S.-origin items with non-U.S. origin items)
  - ZTE obstructed justice by lying/misleading investigators about these transactions, including misleading its own lawyers
  - BIS identified 380 alleged violations of U.S. law



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## Enforcement Trends: ZTE Case, *con't*

- March 8, 2016: BIS added ZTE (and several affiliates)
  - U.S. persons (or within U.S. jurisdiction) require a license from Commerce to send items/data "subject to the EAR" to ZTE
- March 24, 2016: BIS issued a temporary general license authorizing nearly all exports/retransfers to ZTE
- March 2017: BIS and ZTE entered into a settlement agreement wherein BIS issued a denial order against ZTE, but agreed to suspend implementation of the denial order provided ZTE:
  - Pay \$661M in fines (\$300M was suspended)
  - Conduct audits of its compliance program with U.S. export controls
  - Hire an independent corporate compliance monitor
  - Fully cooperate with the U.S. government in carrying-out terms of the settlement
- July 2017 (and November 2016): ZTE stated it disciplined relevant employees
- February 2018: ZTE admits that it had not, actually, disciplined the employees
- April 2018: BIS concludes these false statements fit with a pattern of concealing misconduct and lifts the suspension of the denial order.
- May 9, 2018: ZTE announces it has halted major operating activities
- May 13, 2018: Trump tweets that he and President Xi of China are working together to get ZTE "back into business." He continued, "[t]oo many jobs lost. Commerce Department has been instructed to get it done!"



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## Enforcement Trends

- FLIR Systems: \$30M settlement for ITAR violations
  - Submitted 18 voluntary disclosures related to these issues
  - 347 charges of violating the ITAR
    - Unauthorized exports of technical data / defense services
    - Violating provisos on approved transactions
    - Failing to maintain records
  - Suspend \$15M in penalties on condition spent on compliance
- FedEx: \$500K civil penalty to BIS
  - 53 alleged violations of the EAR
  - Attempted unlicensed exports to entities on U.S. screening lists
  - Items totaled \$58K and were 9A991 and 7A994



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## OFAC Regulations

- Broad sanctions against certain nations supporting terrorism
- 31 CFR Part 500 – 598
- Total embargos or “Country-Based Sanctions”
- Economic sanctions or “List-Based Sanctions”
- Need to regularly update country lists
- Penalties:
  - Criminal fine: \$100,000 to \$20,000,000 and up to 30 years in prison
  - Civil Fine: \$284,582



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# Country-Based Sanctions

## Embargoes/Sanctions are in place for:

- Balkans
- Belarus
- Burundi
- Central African Republic
- Cuba
- Democratic Republic of the Congo
- Iran
- Iraq
- Lebanon
- Libya
- North Korea
- Somalia
- ~~Sudan~~
- Syria
- Ukraine/Russia
- Venezuela
- Yemen
- Zimbabwe



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## OFAC Update - Cuba

- **Background:** broad country-based sanctions against Cuba
  - Commercial, economic, and financial
- **December 2014: Charting a new course on Cuba...**
  - Open diplomatic relations with Cuba
  - Allow for travel to Cuba for 12 categories
  - Allow for export of certain goods/services to Cuba
  - Allow for certain financial transactions to facilitate authorized transactions
- **June 2017:... Or not**
  - Limit the allowable travel
  - Expand list of forbidden Cuban entities
  - General policy of denial on export applications
  - No direct financial transactions



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## OFAC Update - Iran

- Background: Comprehensive economic sanctions against Iran, beginning in 1979 and evolving through 2015
- January 2016: Joint Comprehensive Plan Of Action (JCPOA)
  - Provides for certain sanctions relief in exchange for assurances regarding a peaceful, civilian in nature, nuclear program
    - Allow Iranian banks access to certain currency exchanges, establish subsidiaries in Europe, etc
    - Remove dozens of names from the U.S. Specially Designated Nationals List
    - Waiving/suspending secondary sanctions on non-U.S. persons
    - General License H: permits foreign subsidiaries of U.S. companies to engage in transactions involving Iran
    - Favorable licensing policy for commercial aviation
- May 8, 2018: hard exit from the JCPOA
  - 90-day to 180-day wind-down periods (not grace periods)



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## Foreign Corrupt Practices Act – Generally

- Key Provisions
  - Foreign Payments Provision – DOJ
    - Prohibits U.S. companies from making “corrupt payments” to “foreign officials” “to get business”
  - Accounting Provisions – SEC
    - Requires companies whose securities are listed in the U.S. to keep accurate records that “fairly” represent transactions.



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## Foreign Corrupt Practices Act – Generally

- **U.S. Companies:**
  - U.S. Citizen, national, resident, or in the U.S.
  - Company organized in the U.S. or principle place of business in the U.S.
  - Part of the act took place in the U.S.
- **Payment:** anything of value (including offers or promises)
  - No materiality required
- **Foreign official:** government employee or representatives, political party (including candidates)
- **Corrupt:** attempting to influence the recipient to misuse their official position
- **“To get business”:** may also be to obtain a business advantage



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## FCPA Update

- Fairly typical year for FCPA enforcement
- Continuing to focus on individuals within organizations
- DoJ Formalizes FCPA Corporate Enforcement Pilot Program
  - Encouraging voluntary disclosures by giving “markedly less” credit to companies that do not voluntarily disclose FCPA violations
    - Range of 25-50 percent from the bottom of the applicable guidelines range with a full voluntary disclosure plus cooperation
- Greater global cooperation
- April 2018: Panasonic \$280M settlement
  - \$143M to SEC and \$137M to DoJ



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## Conclusion

- Constant changes in the export regulations
  - Export Control Reform
  - Sanction / Embargoes (often based on foreign relations issues)
- China is a focus of the U.S. government
- Understand the evolving regulations and focus on compliance
- The regulations are not going away
  - Expect more changes to come



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*Lombardo Law PC is based in Southern California and specializes in U.S. Export Controls and Government Contracts.*



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