Voluntary Self-Disclosures - An Important Tool for Dealing With Export Violations

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It's a problem that arises in many companies – you suddenly discover that an export violation may have occurred within your company. It might be a low level violation or it may be a more serious problem, such as the disclosure of controlled technical data to a foreign national without a license, sales to a restricted country or to a restricted party. Perhaps you are not sure if a violation has occurred or if your company is at fault. If handled quickly and properly, most export violations can be resolved effectively with minimal impact on the company. If not dealt with properly, they can lead to significant legal exposure for the company and its employees and long term disruption to your business. This is especially the case if the violation is ongoing – the longer a violation continues the greater the legal danger becomes.

Penalties for export violations are serious – violations under the Export Administration Regulations ("EAR"), International Traffic In Arms Regulations ("ITAR") and OFAC sanctions programs can result in civil and criminal penalties, with financial fines of up to $1,000,000 and 20 years imprisonment per violation. Penalties can be assessed on the company as well as on individuals in their personal capacities including employees, officers and directors. Each of the Bureau of Industry and Security ("BIS"), Directorate of Defense Trade Controls ("DDTC"), Office of Foreign Assets Control ("OFAC") and the Justice Department have robust enforcement offices which announce civil export enforcement actions or criminal prosecutions on a regular basis.

There are a number of important steps to consider if you discover a potential export violation (for a detailed discussion of these steps see: Dealing With Violations In Export and Import Transactions.) However one important option that is frequently available to the exporter is the submission of a voluntary self-disclosure. Under a voluntary self-disclosure, the company submits a statement to the government agency involved describing the possible violation and details behind the incident. The agency then reviews the submission, assess the seriousness of the issue and the steps taken by the company to deal with the violation, and determines a proper response. If the agency concludes that the violation was inadvertent and the company is motivated to avoid future violations, the agency can impose no penalties on the company and resolve the violation. Even if the agency concludes that the company was at fault for serious wrongdoing, a voluntary self-disclosure is considered a "mitigating factor" in assessing penalties and the agency can reduce the penalty that is imposed based on the fact that the company voluntarily disclosed the violation.[1]

Each of BIS, DDTC and OFAC has its own program for submitting voluntary self-disclosures. (DDTC refers to such disclosures as "voluntary disclosures.") In addition, the Justice Department's National Security Division has issued guidance that companies are permitted to submit voluntary self-disclosures directly to the Justice Department for criminal violations of the export control laws (discussed further below).

Factors In Considering A Voluntary Self-Disclosure. The decision regarding whether to submit a voluntary self-disclosure is a complex legal question. Export control officials have stated publicly that if a company submits a voluntary self-disclosure, this can reduce the likelihood of a criminal referral to the Justice Department and often results in reduced or no penalties. In addition, it provides the opportunity for your company to tell its side of the story and introduce favorable information such as mitigating factors and corrective steps that the company has taken since the violation. As such, a voluntary self-disclosure can be valuable in minimizing the impact of a violation. However, companies also surrender valuable legal rights in this process. In addition, companies must be extremely careful in providing confidential information to a government agency unless the company will obtain a valuable benefit in return. You should carefully review with your legal counsel whether the facts of your situation are suitable for a voluntary self-disclosure and the likelihood of success in your particular case.

Factors Considered By the Reviewing Agencies. In reviewing voluntary self-disclosures the agencies consider a number of factors including: (i) whether the violation was willful and reckless; (ii) whether the company's senior officers were aware of the conduct giving rise to the violation; (iii) whether the violation resulted in harm to the agency's regulatory program resources; (iv) individual characteristics of the company, such as its size of operations, commercial sophistication (agencies will often expect larger companies to have more sophisticated export compliance operations); (v) whether the company had an export compliance program; (vi) the actions the company has taken to assure that the violation will not happen again; (vii) whether the company cooperated with the agency in resolving the violation; and (viii) whether there were multiple unrelated violations or enforcement actions. Both BIS and OFAC have issued Enforcement Guidelines that describe factors that the agencies consider in assessing civil penalties, including providing mitigation credit for submitting voluntary self-disclosures.

Actions that the agencies can take in response to a voluntary self-disclosure include taking no action related to the violation, issuing a warning or "cautionary" letter without assessing a penalty, requesting additional information, imposing a penalty (although as referenced above voluntary self-disclosures are considered a "mitigating factor" that frequently result in reduced penalties),[2] criminal referral and other administrative actions.

Key Issues To Address. In submitting a voluntary self-disclosure, the company should describe all significant facts related to the violation and provide copies of supporting documents. In addition, it is important to describe all relevant mitigating factors such as if the company was not aware that the action in question was a violation when it occurred, and as soon as it realized that a violation occurred it stopped the wrongful action. Further, the company should describe the steps it has taken following the violation to assure that the problem will not occur again in the future. Such steps include, for example, appointing an employee of the company to oversee export compliance within the company, upgrading the company's export compliance program and conducting compliance training for company employees. The key is to demonstrate that, regardless of the seriousness of the incident involved, the company acted properly when it discovered the violation and is taking appropriate steps to prevent similar events in the future.

Disclosures are often submitted in two stages – first an initial disclosure that provides a high-level description of the violation, and second a final disclosure that provides the full details of the incident in question. The initial disclosure provides the company the opportunity to quickly inform the government of the violation. The company is then expected to undertake a thorough review of the facts in question and submit a final report.

Disclosure Must Be Submitted Before Government Learns of the Violation. In most cases, to receive the benefits of the disclosure it must be submitted before the U.S. government learns about the violation. If the company submit the disclosure and the government already knows about the violation in question, the company can lose the mitigation benefits of the disclosure. See, eg., 22 CFR §127.12(b)(2) and 15 CFR §764.5(b)(3).

Mandatory Disclosures. In certain instances disclosure of a violation is a mandatory requirement. For example under ITAR, parties are *required* to submit mandatory disclosures to DDTC for engaging in transactions, submitting marketing proposals or engaging in brokering activity with a "proscribed country" listed in ITAR §126.1, and failing to return ITAR-controlled items to the U.S. that were temporarily exported pursuant to 22 CFR §123.17 (c) and (f) through (i).[3]

Department of Justice Program For Voluntary Self-Disclosures For Criminal Export Violations. As referenced above, export control violations can be criminal as well as civil. The Justice Department National Security Division ("Justice") has issued guidance that companies are permitted to submit voluntary self-disclosures directly to Justice for criminal violations of the export control laws (the "DOJ Guidance"). If a filing company meets the requirements under the DOJ Guidance, it may become eligible for "significantly" reduced penalties including "the possibility of a non-prosecution agreement (NPA), a reduced period of supervised compliance, a reduced fine and forfeiture and no requirement for a monitor."[4] This creates the significant benefit of potentially reducing criminal penalties for a violation, but makes the assessment of filing voluntary self-disclosures more complex. As referenced above, companies often submit initial disclosures to the civil agencies followed up by final disclosures at a later date, and the agencies have the discretion to refer criminal matters to Justice during this period. Under the Justice Department program, companies must consider early in the process if they will also file a voluntary self-disclosure with Justice concurrently with filing the initial voluntary self-disclosures with the civil agencies.

Potential export violations must be dealt with quickly and correctly. In many cases a voluntary self-disclosure can be an effective method for resolving violations, reducing legal risk and cleaning up past problems. However they must be used carefully, based upon the advice of experienced legal counsel addressing the pros and cons in the context of the facts of your particular case. If used properly, they can be an effective tool in your export compliance took kit.

Note: This article contains general, condensed summaries of actual legal matters, statutes and opinions for information and education purposes. It is not intended and should not be construed as legal advice.

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[1] See, eg., 15 CFR §764.5(a) which identifies voluntary self-disclosures as a mitigating factor in assessing EAR violations. However see also 15 CFR §764.5(b)(4) which provides that the mitigating effect of a voluntary self-disclosure may be outweighed by aggregating factors.

[2] See footnote 1 above.

[3] See 22 CFR §126.1(e)(2) and §123.17(j).

[4] Under the DOJ Guidance, to receive the benefits of a voluntary self-disclosure, the submission must be made on a timely basis, must disclose all of the relevant facts and must be submitted "prior to an imminent threat of disclosure or government investigation." (citing U.S.S.G. §8C2.5(g)(1)). In addition, the Guidance provides that the submitting party must provide proactive cooperation to Justice in its investigation of the matter and timely and appropriate remediation. If a company meets these criteria, the company can become eligible for "a significantly reduced penalty, to include the possibility of a non-prosecution agreement (NPA), a reduced period of supervises compliance, a reduced fine and forfeiture and no requirement for a monitor." DOJ Guidance p. 8. The DOJ Guidance does not set forth specific levels of relief that will be afforded as in the OFAC and BIS Enforcement Guidlines, but rather states that the ultimate resolution will be determined based upon on an evaluation of the totality of the circumstances in a particular case. If more aggravating circumstances are present, a more stringent resolution will be required. The DOJ Guidance states: "Nevertheless, the company would still find itself in a better position than if it had not submitted a

VDS, cooperated, and remediated." Guidance, p. 9.

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