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## **AN OVERVIEW OF U.S. EXPORT CONTROL LAWS**

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## INTRODUCTION

There is a growing trend for U.S. companies to be involved in some form of international business. Companies which are engaged in exports, overseas licensing, foreign investment or other types of international operations are subject to a complex array of federal laws that regulate international business transactions. Due to the severe civil and often criminal liabilities associated with these laws, they create a significant burden and legal risk for the company. All too often, U.S. firms are unaware of the presence of these laws until it is too late.

The purpose of this Memorandum is to help companies understand the risks and legal obligations that arise under the U.S. export control laws. It will provide an overview of the substantive laws involved in this area and practical steps to take to reduce liability in conducting operations under these laws. Since even the smallest of companies are now often involved in some form of international business, these issues will most likely arise in for a significant number of companies. Such issues will be particularly important in industries which are subject to a high level of regulation under the export control laws such as the technology, computer, software, telecommunications, electronics, energy, defense, chemical and government contracts industries.

There are over 29 federal statutes and regulations which address exports<sup>2</sup>. (Such laws are hereinafter collectively referred to as the "Export Control Laws.") The purpose of these laws is to control exports and re-exports for purposes of national security, foreign policy, short supply, reduction of nuclear proliferation, limitation of chemical or biological warfare, antiterrorism, crime control, enforcement of economic embargoes, compliance with United Nations resolutions and other purposes. These laws apply to both the export of tangible products as well as the export of technology, technical data, software, trade secrets and similar types of information. These programs are administered on an uncoordinated basis by at least 16 federal agencies. Sanctions for violations include civil and criminal penalties - criminal sanctions are often imposed on both corporate defendants as well as officers, directors and employees of the corporation in their personal capacities.

The principal federal authorities for export controls are: (i) the Export Administration Regulations; (ii) the Arms Export Control Act; and (iii) various embargoes administered under the U.S. Sanctions Programs. In addition, there are numerous other federal statutes which address the export of specific products or are in the context of specialized industries such as transportation, vessels and watercraft, chemicals and hazardous materials, electric power, narcotics and dangerous drugs, agriculture and endangered fish and wildlife. A listing of these statutes and regulations is set forth as Appendix A.

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<sup>2</sup> A partial listing of these statutes and regulations is set forth as Appendix A.



A. The Export Administration Regulations (15 CFR §§ 730 et seq.)

1. Introduction. The principal program for the federal regulation of exports is under the Export Administration Regulations (“EARs”). See 15 C.F.R. §§ 730 to 744. The EARs control the export and re-export of U.S.-origin products and technologies from the United States. The Regulations were initially adopted pursuant to the Export Administration Act and are administered by the U.S. Department of Commerce (“Commerce”). The EARs prohibit the export of certain goods, software and technologies identified therein to specific foreign countries or require exporters to obtain export licenses for the export of such items.
2. Commerce Control List. The EARs incorporate a list of approximately 3,000 items (the "Commerce Control List" or “CCL”) which are subject to export restrictions. Items on the CCL are prohibited from export to certain destinations unless an export license is issued by Commerce. Items on the CCL include products, software required to operate such products and technology related to such products. Examples of products which are subject to export licensing include electronic navigation control systems, computer aided design devices (CAD-CAM), high performance computers, network components (routers, hubs, servers), computerized telecommunications switches and high performance composite materials.
3. Dual Use Items. Items which are “dual use,” i.e., which can be used in both military and civilian applications, will often be restricted from export as a result of the potential for their use abroad in a military context. Under this principle, items which are often widely in use in civilian commerce within the U.S. are restricted from export due to their potential military use abroad.
4. End-Use Based Controls. In addition to CCL-based export controls, the EARs prohibit the export of any product, software or technology which will be used in any of the prohibited end-uses set forth in 15 CFR § 744 (the "Prohibited End-Uses"). The EARs also prohibit the performance of any services which are in furtherance of the Prohibited End-Uses. The Prohibited End-Uses include activities related to the following:
  - (a) Encryption Devices;
  - (b) Nuclear Explosive Activities;



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- (c) Missiles;
- (d) Chemical or Biological Weapons;
- (e) Foreign Maritime Nuclear Propulsion Projects;
- (f) Certain Exports to Foreign Vessels;
- (g) Products or Technology to be used in the manufacture or refurbishment of Libyan aircraft.

This section also prohibits U.S. parties from entering into export transactions with parties on the Entities List set forth under Section 744 (the "Prohibited End-Users"). The Prohibited End-Users include:

- (a) Certain Russian entities listed at 15 C.F.R. Part 744, Supplement 4;
- (b) Certain Indian and Pakistani governmental, military, parastatal and private entities listed at 15 C.F.R. Part 744, Supplement 4;
- (c) Certain persons and entities identified at 31 C.F.R. part 595, Appendices A-C.

This category of controls applies not just to items which are specifically identified (such as items listed in the CCL), but to effectively all items which the exporter knew or reasonably should have known would be used in connection with the Prohibited End-Use. This restriction is considerably broader in scope than restrictions for products which are listed on the CCL. Exports of the above items are either flatly prohibited or subject to the licensing or other restrictions set forth at 15 C.F.R. Part 744.

- 5. Re-exports. In addition to controlling exports from the United States, the EARs control the "re-export" of products manufactured in foreign countries which incorporate U.S. components or which are based upon U.S.-origin technology.
- 6. Software and Technology. The EARs apply to the export of products as well as software, technology and other types of information.
  - (a) Exports of software and technology are "deemed" to occur by: (i) transporting information out of the U.S. by mail, courier or similar



means; (ii) traveling abroad and releasing information in a foreign location through oral or written means or through personal demonstration; or (iii) releasing information to foreign nationals in the United States.

- (b) Thus electronic sales/licensing of software, electronic posting of technical manuals, electronic transmission of education materials, and even e-mails, fax and telephone calls constitute exports if foreign nationals can have access to such materials.
- (c) Posting such items in chatrooms, “intranets” or the Internet or storing items in computer networks constitute an export if a foreign national can have access to such items.

7. Regulatory Requirements For All Exports. In addition, U.S. companies are required to follow certain procedures for all export transactions, even if the transaction does not require an export license:

- (a) Recordkeeping requirements – U.S. parties are required to maintain records of exports for five years including documents set forth at 15 C.F.R. § 762.
- (b) Denied Persons List – U.S. persons are prohibited from exporting to parties which have been convicted of export violations (See 15 C.F.R. § 764.); U.S. exporters must review the Denied Persons List prior to all exports.
- (c) Filing Shippers Export Declarations and Other Export Control Documents – parties are required to file certain export clearance documents upon export such as Shipper's Export Declarations. See 15 C.F.R. § 758.

8. Penalties. Violations of the EARs can result in severe sanctions including up to 20 years imprisonment and civil penalties of \$250,000 per violation or twice the value of the transaction that is the basis of the violation.

9. Enforcement Priorities. The highest priority of enforcement is in the areas of computers and technology products, telecommunications, aerospace and navigation, high performance materials, chemicals, biological products and nuclear materials.



B. U.S. Sanctions Programs (31 C.F.R. Chapter V)

1. Introduction. The United States maintains economic embargoes against a number of foreign countries under the International Emergency Economic Powers Act (“IEEPA”),<sup>3</sup> the Trading With the Enemy Act (“TWEA”),<sup>4</sup> the International Security and Development Cooperation Act of 1985 and related statutes,<sup>5</sup> the United Nations Participation Act,<sup>6</sup> the Iraqi Sanctions Act,<sup>7</sup> the Cuban Democracy Act,<sup>8</sup> the Cuban Liberty and Democratic Solidarity Act of 1996,<sup>9</sup> the Antiterrorism and Effective Death Penalty Act of 1996,<sup>10</sup> as well as a number of Executive Orders. The purpose of these embargoes is to further the foreign policy interests of the United States and to fulfill our obligations under various United Nations Security Council resolutions. These prohibit, with certain exceptions, a broad array of commercial dealings between U.S. persons and parties in the embargoed countries. These embargoes, referred to herein as the “U.S. Sanctions Programs,” are administered primarily by the Office of Foreign Assets Control (“OFAC”) within the Department of the Treasury (“Treasury”), in conjunction with Commerce and State.
2. Countries Covered. A few years ago sanctions were applied to only a few “black listed” countries such as Iran, North Korea and Cuba. Within recent years, however, sanctions have been expanded by OFAC to cover a larger number of countries and sanctions programs.
3. Comprehensive Sanctions. The exact terms of the U.S. Sanctions Programs vary for each of the OFAC programs. Generally speaking, there are two types of sanctions programs currently in effect: comprehensive programs and limited programs. Under the comprehensive U.S. Sanctions Programs, U.S. persons are prohibited from engaging in a broad array of commercial dealings (with certain exceptions) with persons in the embargoed countries often including exporting or importing products, performing services, making investments, payments, or other financial transactions with persons in a sanctioned country, or engaging in any other commercial activity with persons in that country. In some cases, U.S.

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<sup>3</sup> 50 U.S.C. A. §§ 1701-1706 (1998).

<sup>4</sup> 50 U.S.C. A. §§ 1-44 (1998).

<sup>5</sup> 22 U.S.C. A. § 234999-9 (1998).

<sup>6</sup> 22 U.S.C. A. § 287c (1998).

<sup>7</sup> Pub. L. No. 101-513, 104 Stat. 2047-55.

<sup>8</sup> 22 U.S.C. A. § 6001-6010 (1998).

<sup>9</sup> Pub. L. No. 104-114.

<sup>10</sup> Pub. L. No. 104-132.



persons are prohibited from even providing advice on methods to circumvent the embargo. Examples of comprehensive sanctions programs are the major embargo programs related to Iran, Cuba, North Korea and Sudan.

4. Limited Sanctions. Under limited sanctions programs, U.S. persons are prohibited from engaging in specifically identified types of commercial activities designated under the sanctions program for particular countries, but are free to conduct other types of commercial activities with nationals of such countries.
5. Extraterritorial Application. In many cases, the U.S. Sanctions Programs apply to “U.S. Persons” and foreign subsidiaries and other affiliates of such persons if they are “owned or controlled” by a U.S. person. In determining whether a foreign affiliate of a U.S. company constitutes an “owned or controlled” foreign firm for purposes of the U.S. Sanctions, OFAC may look at such factors as stock ownership, voting control arrangements or parent company participation on the board of directors. In general, practical working control is considered to be “control” for purposes of the Sanctions Programs. Many of the U.S. embargoes are applied on an “extraterritorial” basis. This means that the U.S. Government will attempt to regulate the transfer of products or technologies from one foreign location to another if they are under the control of a foreign corporation if such corporation is under the direct or indirect control of a U.S. party. This is even if such product or technology did not originate in the United States, or was not developed based upon U.S.-origin goods or technology.
6. Entity Based Sanctions. OFAC also maintains a system of sanctions called “List Based Sanctions” which create a significant additional compliance obligation for U.S. companies. Under this system, in addition to imposing sanctions on a particular country (e.g., Iran), OFAC has developed lists of persons and business entities (such as corporations and partnerships) which are connected with embargoed countries or otherwise targeted by the US Government. Under OFAC regulations U.S. persons are prohibited from conducting business with parties identified on these entities lists anywhere in the world. Thus if a company based in London is partially owned by Iranian nationals and the company is placed on an “entity-based” sanctions list, U.S. persons are prohibited from conducting business with this entity anywhere in the world. OFAC has developed a number of such lists (hereinafter referred to collectively as the “List of Specially Designated Nationals” or “SDN Lists”) which include



approximately 3,000 parties. See 31 C.F.R. § Chapter V. U.S. US persons are strictly prohibited from entering transactions with parties set forth on the SDN Lists. Many companies have adopted compliance programs which conduct reviews of their business transactions on either a computerized or a manual basis that verify that they are not conducting transactions with parties listed on the SDN Lists.

7. Penalties. Penalties for violations of provisions of the U.S. Sanctions Programs include imprisonment for up to 20 years and civil penalties of up to \$250,000 per violation or twice the value of the transaction that is the basis of the violation.

C. The Arms Export Control Act (International Traffic In Arms Regulations)

1. Introduction. A third major export control program is pursuant to the Arms Export Control Act<sup>11</sup> and the International Traffic in Arms Regulations (“ITAR’s”)<sup>12</sup> promulgated thereunder. This program regulates the export of goods, services, software and technical data which have the potential for use in a military context. The ITAR’s are administered by the Directorate of Defense Trade Controls (“DTC”), an agency within the U.S. Department of State (“State”).
2. Regulation of Defense Articles. An item or service is regulated under the ITAR’s if it is considered a “Defense Article.”<sup>13</sup> Generally, an item or service is a Defense Article if it was originally developed for a military use or has a significant military application. It is important to note that even if a product has widespread civilian uses, it may still be considered a Defense Article if it was originally developed for military use. If an item is controlled as a Defense Article or a related technology or service, it is restricted from export unless an export license is issued by the State Department. Exporters of Defense Articles are also subject to additional restrictions such as obtaining delivery verification documentation, maintaining records of exports and filing reports with the State Department.
3. U.S. Munitions List. The ITAR’s contain a detailed list of items which are deemed to be Defense Articles. This is referred to as the U.S. Munitions

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<sup>11</sup> 22 U.S.C.A. §§ 2778-2799.

<sup>12</sup> 22 C.F.R. §§ 120-130.

<sup>13</sup> The term “defense article” is defined in 22 C.F.R. § 120.3.



List.<sup>14</sup> The Munitions List sets forth 21 categories of items and approximately 2000 specific items subject to export controls. Some of these categories are specific, such as Category VI - Vessels of War and Special Naval Equipment. However, some of the categories are very open-ended such as Category XI - Military Electronics (which covers areas of electronics and computer equipment), and Category XII - Auxiliary Equipment (which covers encryption/cryptography equipment). The broadest category is Category XXI - Miscellaneous Articles, which includes any article not “specifically enumerated in the other categories of the U.S. Munitions List which has substantial military applicability and which has been specifically designed or modified for military purposes.”<sup>15</sup> The decision on whether any article may be included in this category is made by the Director of the Office of Defense Trade Controls. These open-ended categories reserve great discretion to the State Department to add other items to the Munitions List as it sees fit on an ongoing basis.

4. Software and Technology. The Munitions List covers both “hard goods” as well as technical data “directly related to Defense Articles.”<sup>16</sup> Technical data include software, designs, know-how, drawings, training information and other types of information which are related to the specified Defense Articles.
5. Defense Services. In addition, the ITAR applies to “Defense Services,” i.e. the furnishing of assistance, including training, to foreign persons related to the design, development, maintenance or use of Defense Articles. Parties are prohibited from performing Defense Services for foreign parties to the same extent that they are prohibited from selling the Defense Articles which relate to such services.
6. Overlap With Export Administration Regulations. The EARs and the ITAR’s are complementary and often-times overlapping regulations, and should be read in conjunction with each other. In some cases an export license may not be required under the EARs, but because the product will be used for a military end-use or has a predominant military application, an export license is required under the ITAR’s. As with the EARs, the term “export” is broadly construed to include access of data in the U.S. by foreign individuals, plant visits and technical presentations.<sup>17</sup>

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<sup>14</sup> The Munitions List is set out at 22 C.F.R. § 121.

<sup>15</sup> Id.

<sup>16</sup> 22 C.F.R. § 121.1 Category VI (d).

<sup>17</sup> 22 C.F.R. § 120. 17.



7. Registration As A Munitions Manufacturer. In addition to the requirements described above, the ITAR requires manufacturers of Defense Articles to register as munitions manufacturers (“Munitions Manufacturers”) regardless of whether or not they contemplate an export. (See 22 C.F.R. Part 122.) Other requirements such as disclosure of certain political contributions and commissions paid to secure the sale of Defense Articles apply to registered Munitions Manufacturers.
8. Registration As Munitions Broker. Parties that serve as sales agents in selling Defense Articles or related technologies or services are required to register with DTC as munitions brokers.
9. License Certifications. Applicants for export licenses issued by DTC are required to certify that none of the parties to the transactions, including third party agents, have violated various U.S. export statutes and other national security priorities. This restriction also requires that the license applicant certify that none of the parties to the transaction have violated relevant export control statutes.
10. Sanctions. Sanctions for violations under the ITARs include imprisonment for up to 10 years and fines of up to \$50,000 per transaction.

D. Other Export Statutes

1. Additional Export Regulatory Requirements. In addition to the three export regulatory programs described above, there are additional U.S. export statutes which regulate specific individual classes of products. These specialized classes of products include:
  - (a) Pharmaceuticals
  - (b) Nuclear products
  - (c) Ships and maritime products
  - (d) Toxic substances
  - (e) Chemicals
  - (f) Electric Power



(g) Endangered species

A listing of U.S. export statutes and regulations is set forth as Exhibit A.

E. U.S. Antiboycott Laws

1. Summary of the Law - The restrictive trade practices provisions of the Export Administration Regulations (“EAR Antiboycott Law”) prohibit United States persons from honoring the boycott requests of foreign boycotting nations. Included in the prohibited activities are the refusal (or agreement to refuse) to do business with a boycotted nation, its business organizations and its nationals or residents (“boycott targets”), the taking of discriminatory actions against the boycott targets, and the furnishing of information to boycotting nations pertaining to certain business relationships, race, religion, sex or national origin related to boycott targets. In addition to setting forth these prohibitions, persons who violate the EAR Antiboycott Law are subject to the sanctions set forth in the Export Administration Regulations.
  
2. Prohibited Activities - The EAR Antiboycott Law prohibits United States persons from engaging in the following activities:
  - Refusing to do business with or in a boycotted country, with any business concern organized under the laws of a boycotted country, with any national or resident of a boycotted country, or with any other person, pursuant to an agreement with, a requirement of, or a request from or on behalf of a boycotting country;
  
  - Refusing to employ, or otherwise discriminating against, any United States person on the basis of race, religion, sex or national origin of that person or of any owner, officer, director, or employee of such person when undertaken with the intent to comply with, further or support an unsanctioned foreign boycott;
  
  - Furnishing information with respect to the race, religion, sex or national origin of any United States person or of any employee of such person when undertaken with the intent to comply with, further or support an unsanctioned foreign boycott;



- Furnishing information about whether any person has, has had, or proposes to have any business relationship with or in a boycotted country, with any business concern organized under the laws of a boycotted country, with any national or resident of a boycotted country, or with any other person which is known or believed to be restricted from having any business relationship with or in a boycotting country when undertaken with the intent to comply with, further or support an unsanctioned foreign boycott;
  - Furnishing information about whether any person is a member of, to, or is otherwise associated with or involved in the activities of any charitable or fraternal organization which supports a boycotted country when undertaken with the intent to comply with, further or support an unsanctioned foreign boycott;
  - Paying, honoring, confirming or otherwise implementing a letter of credit which contains any condition or requirement compliance with which is prohibited by the EAR antiboycott law.
3. Exceptions to Prohibitions - There are a number of major exceptions which exist under which U.S. persons may legally comply with foreign boycott requests or restrictions. These are summarized below. The applicability of these exceptions are quite complex, however and parties should consult with legal counsel and the provisions of the EAR's to confirm the applicability of any of the following exceptions to the specific transaction in question.
- Import Requirements of a Boycotting Country. A party which is providing goods or services to a boycotting country is permitted to comply with that country's requirements which prohibit the import of goods or services from a boycotted country. That party may not, however, refuse "on an across the board basis" to do business with the boycotted country or a national or resident thereof. Under this exception, a United States person is limited in the types of boycott related information which he can supply. In addition, a party which is shipping goods to a boycotting country is permitted to comply with that country's requirements which prohibits shipments on a carrier of the boycotted country or by a route other than that prescribed by the boycotting country or the recipient of the shipment.



- *Shipment of Goods To A Foreign Country.* A U.S. person, in shipping goods to a boycotting country, may under certain conditions comply or agree to comply with requirements of that country which prohibit the shipment of goods (i) on a carrier of the boycotted country; or (ii) by a route other than that prescribed by the boycotting country or the recipient of the shipment.
  
- *Import and Shipping Document Requirements.* A party which is shipping goods to a boycotting country may comply with that country's import and shipping document requirements in providing the following information: the country of origin of the goods, the name of the carrier, the route of shipment, the name of the supplier and the name of the provider of other services. Information conveyed pursuant to this exception, however, must be stated in "positive, non-blacklisting, non-exclusionary" terms; negative terms such as "subject cargo did not originate in Israel" are strictly prohibited. Information with respect to the names of carriers or routes of shipment, however, may be stated in negative terms in conjunction with shipments to a boycotting country in order to comply with precautionary requirements protecting against war risks or confiscation.
  
- *Compliance with Unilateral Selection.* Another exception provides that a party is permitted to comply in the normal course of business with a unilateral and specific selection by a boycotting country or a national or resident thereof of carriers, insurers, suppliers of services to be performed within the country or specific goods which in the normal course of business are identifiable as to their origin at the time of entry into the boycotting country. Under this exception, the selection must be specific and unilateral. The terms "specific" and "unilateral" are defined precisely in the EAR's. This exception does not apply, however, to any unilateral selection if the United States person knows or has reason to know that the purpose of the selection is to effect discrimination against any United States person on the basis of race, religion, sex, or national origin.
  
- *Shipment and transshipment of Exports pursuant to a Boycotting Country's Requirements.* A party is permitted to comply with the export requirements of a boycotting country pertaining to shipments or transshipments of exports to a boycotted country, any business concern of a boycotted country or any national or resident



of the boycotted country. A U.S. person may not, however, refuse on an across-the-board basis to do business with a boycotted country or a national or resident of a boycotted country.

- *Immigration, Passport, Visa or Employment Requirements of Boycotting Country*. A U.S. individual is permitted to comply with the immigration, passport, visa or employment requirements of a boycotting country provided that such individual furnishes information only about himself or a member of his family. A U.S. company is not permitted to furnish information about its employees or executives, but may allow these individuals to respond on their own to such requests. Finally, no employees may be selected for work on a project in a boycotting country in advance in a manner designed to comply with a boycott.
  - *Compliance with Local Law* - Under certain circumstances United States persons in foreign countries are allowed to engage in activities which may otherwise be prohibited by the EAR Antiboycott Law if such actions are required under certain local laws of the host country.
  - *Activities Exclusively Within a Foreign Country*. A U.S. person who is a bona fide resident of a foreign country, including a boycotting country, may under certain conditions comply or agree to comply with the laws of that country with respect to his activities exclusively within that country.
  - *Compliance With Local Import Law* - A U.S. person who is a bona fide resident of a foreign country, including a boycotting country, may, in importing goods, materials or components into that country, in certain instances comply or agree to comply with the import laws of that country.
4. **Reporting Requirements** - The law requires that any United States person which receives a request for the furnishing of information, the entering into or implementing of agreements or the taking of any other action prohibited under the EAR Antiboycott Law shall be required to report such a request to the Department of Commerce. Parties are required to make these reports on specific forms published by the Department. Forms are to be forwarded to the Department of Commerce in accordance with the instructions set forth in the EAR's.



A request received by a United States person is reportable if that person knows “or has reason to know” that the purpose of the request is to enforce, implement, or otherwise further, support or secure compliance with an unsanctioned foreign boycott or restrictive trade practice. Such a request is required to be reported regardless of whether the action requested is prohibited or permissible under the EAR Antiboycott provisions. Certain narrow exceptions to this reporting requirement are set forth in the law. This reporting requirement applies to all United States persons, but only pertains to transactions or activities which are in the interstate or foreign commerce of the United States.

5. Evasion - The Export Administration Regulations prohibit United States persons from engaging in any transaction or taking any action with the intent to evade the antiboycott laws. In addition, the use of “dummy corporations” or other “devices” to mask prohibited activity will also be regarded as evasion. The evasion provision states, however, that alteration of “a person’s structure or method of doing business” will not constitute evasion as long as the alteration is based on “legitimate business considerations” and “is not undertaken solely to avoid the application of the (antiboycott) prohibitions”. Finally, it is provided that the facts and circumstances of questionable transactions will be carefully scrutinized to determine “whether appearances conform to reality.”
6. Antiboycott Tax Laws. The U.S. Internal Revenue Code also imposes antiboycott prohibitions. (“IRC Antiboycott Law”). These are separate from but similar in nature to the EAR antiboycott provisions. Failure to comply with the IRC antiboycott provisions could result in tax-related penalties as well as other sanctions. The IRC Antiboycott Law also imposes certain reporting requirements which are separate from the EAR Antiboycott Law. Questions regarding these provisions should be addressed to the Company’s tax advisors or the ECA.
7. Sanctions - Sanctions for violations of the EAR Antiboycott Law include the criminal and civil penalties applicable under the EAR’s described in Section II. A. above.

F. Export Compliance Programs

1. Compliance Systems. Executive and judicial branch authorities have held that adoption of formalized company-wide compliance programs are strongly encouraged to assist in compliance with the export control laws.



Such programs help assure that the company's management and employees are aware of applicable laws and are organized to take steps to comply with them. Equally as important, such programs can serve as evidence of the good-faith attempts of management to educate employees and comply with the law. Such evidence can be valuable in defending against claims in enforcement actions that a company did not use reasonable care in complying with the law, or that actions did not reach the level of intentional wrongdoing required to be proven for certain criminal convictions.

2. Substantive Laws Covered – A company's international compliance program is usually centered around the particular international business laws which are most prevalent in its industry. For most companies this would be the Export Administration Regulations and the Foreign Corrupt Practices Act. In the defense industry this would also include the Arms Export Control Act, the International Trafficking in Arms Regulations and various government contracting statutes. In the chemical industry this would include the import/export provisions under the Toxic Substances Control Act, and in the pharmaceutical industry the import/export provisions of the Food, Drug and Cosmetic Act. Most companies also require that their operations in foreign countries be in compliance with the local laws of the foreign jurisdiction. Our recommendation in almost all cases is that in developing an international compliance program, a company should address all relevant substantive laws that impact on its international business activities. This will assure a comprehensive level of control and reinforce the organization's company-wide culture toward legal compliance. A checklist of substantive laws to be included in an international business compliance program is as follows:



## **Substantive Laws To Be Covered In International Business Compliance Program**

### General International Business Laws

- Export Administration Regulations (including export licensing and antiboycott regulations).
- Foreign Corrupt Practices Act.
- Various U.S. sanctions programs administered by the Office of Foreign Assets Control, pursuant to separate Congressional action and United Nations resolution. A list of the 33 full or partial U.S. sanctions provisions is attached hereto as Exhibit A.
- Arms Export Control Act and the ITAR.
- Antiboycott laws set forth in the Internal Revenue Code, 50 App. USC § § 2407.

### Specialized Export Laws (If applicable to company operations)

- Specialized laws related to industries such as maritime and shipping, chemicals, banking, atomic energy, electric power, pharmaceuticals, firearms. A listing of 16 U.S. export control laws is attached as Exhibit A.

### Import Laws (If applicable to company operations)

- Import laws under the Customs statutes and regulations.
- Specialized import provisions under ITAR and Treasury regulations related to alcoholic beverages, tobacco, firearms.

### Foreign Laws

- Laws of the foreign country in which company is operating

3. Parties Covered Under The Program – The international business compliance program should cover all employees of the company involved in international activities, as well as all senior executives of the company.



In addition, companies often require the following parties to comply with the company's compliance program as a condition of the company conducting business with them.

- Outside consultants, advisors, independent contractors.
- Foreign distributors, agents, sales representatives and other business intermediaries.
- Joint venture partners and similar parties, especially if such parties will have access to restricted commodities, software or technology of the company.

4. Relevant Legal Standard - Companies should incorporate legal principles from three general areas of law in their international compliance programs:

- (a) The substantive laws covered under the program (e.g., the Export Administration Regulations, the Foreign Corrupt Practices Act, etc.);
- (b) The emerging legal principles regarding corporate legal compliance programs such as set forth in the Caremark case; and
- (c) The principles set forth in the Federal Criminal Sentencing Guidelines. (The Federal Criminal Sentencing Guidelines do not apply to convictions under certain of the U.S. export laws but courts often apply these principles even if not technically required to do so.)

In the area of the export control laws, U.S. companies are held to a high legal standard for compliance. Sanctions for violations include criminal and civil penalties including up to ten years imprisonment and fines of up to \$1 million per violation.

Civil penalties can be imposed on a strict liability basis, *i.e.*, without any intentional wrongdoing.<sup>18</sup> Criminal sanctions can be imposed for "knowing" violations, although criminal sanctions have also been imposed

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<sup>18</sup> See Iran Air v. Kugelman, 966 F.2d 1253, 1993.



on a strict liability basis.<sup>19</sup> See 15 C.F.R. § 764.2. Under the Export Administration Regulations, the term "knowledge" includes not only positive knowledge that a circumstance exists, but also an awareness of a high probability of its existence or future occurrence. Such awareness is inferred from evidence of the conscious disregard of facts known to a person and is also inferred from a person's willful avoidance of the facts. See 15 C.F.R. § 772. Parties are deemed to have knowledge of the requirements under the export control laws. Ignorance of the law or avoidance of the facts of a particular situation is not a defense.

Criminal sanctions for corporate violations are often imposed on officers, directors and employees of the corporation in their personal capacities as well as against corporate defendants. Sanctions are imposed both for direct participation in violations, as well as failure to properly supervise subordinates.<sup>20</sup>

In addition, violations of these laws encompass not just making prohibited exports but also aiding and abetting, conspiring with or "supporting" other parties who make prohibited exports. Consequently, parties who provide services related to international business transactions, such as transportation, financing, freight forwarding, customs brokering and other facilitation activities, fall within the scope of these laws. This would also include parties who provide information-related products and services such as software or data processing services. If these parties have knowledge of, or reasonably should know, of export violations in transactions in which they are involved, they will also be in violation of the laws set out above.

Sanctions for violations by exporters, carriers and transportation facilitators also include seizure of cargoes and vessels used in such exports under "forfeiture" procedures. These procedures are civil in rem proceedings and hence are subject to a lower burden of proof than criminal enforcement proceedings. See 19 C.F.R. § 162.21.

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<sup>19</sup> See United States v. Shetterly, 971 F.2d 67, 73 (7th Cir. 1992) (holding that 50 U.S.C. App. § 2410(a) requires only that the criminal defendant "knowingly exported . . . a controlled commodity, without obtaining the appropriate export license" and does not require that "the exporter know that a license is required"); cf. Morisette v. United States, 342 U.S. 246, (1952) ("approv[ing]," as constitutional, imposition of strict criminal liability for "public welfare offenses").

<sup>20</sup> For example, in SEC v. Triton Energy Corporation, et al. Civ. Action No. 1:97, C000401 (D.D.C. Feb. 27, 1997), enforcement actions were initiated against the President and the chief financial officer of the defendant corporation in their personal capacities on the grounds that they received information that subordinates were involved in activities which were potentially unlawful but took no action to investigate or stop it.



An example of a typical export control enforcement case is *United States v. Ronald J. Hoffman*, 10 F.3d 808 (1993 9th 1993). In this case, a scientist had developed a software program to measure the effects of rocket plumes emitted from rocket nozzles. The program had applications in both the military and private commercial aerospace markets. The U.S. government learned that Hoffman was attempting to export the program to Germany and South Africa without an export license and began an undercover investigation. Hoffman was arrested and charged with violation of export control laws. He was convicted of criminal violations on all counts following a trial and sentenced to prison. The Court of Appeals affirmed the conviction and sentence.

5. Elements of The Compliance Program. The components of an international business compliance program will vary based upon factors such as the size of the company, the foreign countries in which it operates, the level of regulation in its industry and its past compliance history. However, all compliance plans should incorporate a number of elements which are vital to the compliance effort. There are:
  - (a) Adoption At Senior Company Level: The program must be adopted at the highest levels of the company, preferably by the board of directors or an executive officer. Such adoption should be evidenced by a resolution or similar directive to demonstrate a formalized action by the company.
  - (b) Compliance Official: A person must be identified in the company to be responsible for the program and in charge of overseeing its operations on an ongoing basis. Such person should direct the operations of the program, answer inquiries from company personnel and take appropriate steps in the event of suspected violations.
  - (c) Written Materials: The elements of the program should be set forth in a written document. Usually this consists of an internal management procedure specifying rules and procedures to be followed by company personnel. In addition, these also include educational materials to be distributed to employees which explain the relevant laws and the company's procedures for complying with them.



- (d) Education: An important part of the program is an organized, ongoing program of education for company employees. This consists of more than just the distribution of written materials and often includes training classes, training videos, discussion groups, testing, and other forms of training interaction. Employees should be trained in (i) the relevant laws covered under the program; and (ii) company policies to comply with such laws.
- (e) Update Function: The company must monitor changes in the law and update the program as changes in the law or company operations dictate.
- (f) Periodic Audit: The program should require program administrators to periodically audit or review company operations to verify that personnel are complying with the program.
- (g) Enforcement: If an employee is found to have violated the program he should be sanctioned in accordance with company policy. A program without "teeth" is not considered to be effective.
- (h) Mechanism For Dealing With Suspected Violations: There should be an established procedure for dealing with suspected violations of the program or the law. To begin, employees should be encouraged to report any suspected violations to the compliance officer. In the event of a suspected violation, the administrator, usually in conjunction with corporate counsel, should investigate the claim. Depending on the outcome, the company should take appropriate follow-up steps including ceasing any ongoing activities which may be in violation of the law, sanctioning the employee, consulting outside counsel to conduct an independent investigation, etc.
- (i) Recordkeeping: One of the most widely overlooked areas of international business compliance is recordkeeping. The U.S. international business laws present a significant array of complex recordkeeping requirements for U.S. firms. For example, under 15 C.F.R. § 762 U.S. exporters are required to maintain copies of all documents utilized in their export transaction for five years. Other requirements exist under the U.S. sanctions programs and the U.S. Customs laws. Compliance programs should address the collection and retention of records as an important part of the compliance effort.



G. Steps To Take If An Export Violation Is Discovered.

If a company discovers a violation of the Export Control Laws, it has a number of options available to it based upon whether the violation had occurred in the past and is concluded or if it is an ongoing violation. Actions to be taken in these instances include the following.

1. Ongoing Violations. The following steps should be taken if an ongoing violation of an Export Control Law is discovered.
  - (a) Cessation of Illegal Activity. The activity giving rise to the illegal activity should be stopped immediately.
  - (b) Internal Investigation. It is common in the discovery of export violations for the company to conduct an internal investigation to assess the facts of the violation, the potential legal exposure to the company and steps to take for the company's legal defense. It is imperative that such investigations be structured so that the results become covered under the attorney/client privilege.
  - (c) Reporting of Past Violations. Most Export Control Laws do not set forth any obligations to report past violations provided that they are no longer occurring.
  - (d) Voluntary Disclosure. The company should consider the merits of voluntary disclosure to the Commerce Department or other applicable agencies to mitigate compliance penalties.
  - (e) Compliance Program. The company should immediately put in place a formalized Export Compliance Program so that the violations do not occur again.
  
2. Past Violations. If a violation is not ongoing and occurred in the past, the company should take the following steps:
  - (a) Conduct Internal Investigation. It is common in the discovery of export violations for the company to conduct an internal investigation to assess the facts of the violation, the potential legal exposure to the company and steps to take for the company's legal



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defense. It is imperative that such investigations be structured so that the results become covered under the attorney/client privilege.

- (b) Reporting of Past Violations. Most Export Control Laws do not set forth any obligations to report past violations provided that they are no longer occurring.
- (c) Voluntary Disclosure. The company should consider the merits of voluntary disclosure to the Commerce Department or other applicable agencies to mitigate compliance penalties.
- (d) Compliance Program. The company should immediately put in place a formalized Export Compliance Program so that the violations do not occur again.

June 1, 2009



## APPENDIX A

### **U.S. EXPORT CONTROL LAWS**

1. The Export Administration Regulations, 15 C.F.R. §§ 730.1 to 730.10, administered pursuant to the authority under the International Emergency Economic Powers Act, 50 U.S.C. §§ 1701 to 1706 (1998), extending the Export Administration Act, 50 App. U.S.C. §§ 2401 to 2420 (1998).
2. Arms Export Control Act, 22 U.S.C. §§ 2771 to 2781 (1998) and the International Traffic in Arms Regulations promulgated thereunder, 22 C.F.R. §§ 120.1 to 120.29.
3. Embargoes and sanctions programs administered by the Department of The Treasury are authorized pursuant to a number of statutes including:
  - a. International Emergency Economic Powers Act, 50 U.S.C. §§ 1701 to 1706;
  - b. Trading with the Enemy Act, 50 App. U.S.C. §§ 1 to 44 (1998);
  - c. International Security and Development Cooperation Act of 1985, Public Law 99-83, 99 Stat. 190;
  - d. National Emergencies Act Pub. L. 105-123, 90 Stat. 1255;
  - e. United Nations Participation Act, 22 U.S.C. §§ 287 to 287l;
  - f. Foreign Operations, Export Financing, and Related Programs Appropriations Act, Public Law 101-513, 104 Stat. 2047-55; and
  - g. Antiterrorism and Effective Death Penalty Act of 1996, Public Law 104-132, 110 Stat. 1214-1319.

Treasury Regulations for the above embargoes are set forth in Chapter 31 of the C.F.R. The Burmese and Sudan embargoes are set out in Executive Orders at 1997 WL 271517 (Burma Restrictions) and 1997 WL 687995 (Sudan Restrictions).

4. Controls Affecting Maritime Carriers and Related Activities, 46 U.S.C. §§ 222.1 to 221.111 (1998).



5. Shipping Restrictions; North Korea and the Communist-Controlled Area of Vietnam, 44 C.F.R. §§ 403.1 to 403.7.9
6. Toxic Substances Control Act, 15 U.S.C. §§ 2601 to 2629 (1998), 40 C.F.R. § 707 to 707.75.
7. Antiboycott Regulations, 50 App. U.S.C. § 2407 (1998), 15 C.F.R. §§ 760.1 to 760.5; and Internal Revenue Code §§ 999a to 999f (1997).
8. Secrecy of Certain Inventions and Filing Applications in Foreign Countries, 35 U.S.C. §§ 181 188 (1998).
9. Foreign Corrupt Practices Act, 15 U.S.C. § 78dd-1 and 78dd-2 (1998).
10. Nuclear Technology, 10 C.F.R. §§ 110.1 to 110.135.
11. Electric Power, 10 C.F.R. §§ 205.300 to 205.309.
12. Food, Drug and Cosmetic Act, 21 U.S.C. §§ 381 to 383 (1998).
13. Controlled Substances Import and Export Act, 21 U.S.C. §§ 951 to 971 (1998).
14. Endangered Species Act of 1973, 16 U.S.C. §§ 1531 to 1544 (1998).
15. The Migratory Bird Treaty Act, 16 U.S.C. §§ 703 to 712 (1998).
16. The Act for the Protection of Bald and Golden Eagles, 16 U.S.C. §§ 668 to 668d (1998), 50 C.F.R. §§ 17.1 to 17.7.



## APPENDIX B

### **STEPS IN IMPLEMENTING AN EXPORT COMPLIANCE PROGRAM**

#### A. Export Administration Regulations

1. Identify items which require export licenses under EAR (See attached Questionnaire).
  - a. Items on Commerce Control List (15 C.F.R. Part 742)
  - b. Items subject to End Use-based controls (15 C.F.R. Part 744)
  - c. Items subject to chemical weapons controls (15 C.F.R. Part 745)

Classify items and determine export restrictions based upon country chart. (Optional: Obtain DOC classification opinion for EAR 99 items.) Establish license application procedure for above products.

2. Review and classify software, technology and other intellectual property for export licensing requirements.
3. Establish due diligence review procedures under Know Your Customer Guidelines, 15 C.F.R. Part 732.
4. Establish Denied Party List review procedures under 15 C.F.R. Part 764.
5. Establish export clearance procedures under 15 C.F.R. Part 758.
6. Establish export record-keeping procedures under 15 C.F.R. Part 762.

#### B. International Traffic In Arms Regulations

1. Identify items which require export or import licenses under U.S. Munitions List. Establish license application procedure for above products.
2. Review and classify software, technology and other intellectual property for export licensing requirements.
3. Register as Munitions manufacturer under 22 C.F.R. Part 122.
4. Establish export due diligence procedure.



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5. Establish procedures for reporting payments of sales commissions to agents and political contributions under 22 C.F.R. § 130.9.
6. Establish procedure for complying with record-keeping requirements set forth at 22 C.F.R. § 122.5.
7. Register defense brokers if applicable.

C. U.S. Sanctions And Embargoes

1. Identify company transactions which pose risk of involvement in countries subject to sanctions programs administered by:
  - a. Office of Foreign Assets Control (31 C.F.R. Part V)
  - b. Department of Commerce (15 C.F.R. § 746)
  - c. State Department (22 C.F.R. Part 126)
2. Establish procedure for conducting Specially Designated Nationals List reviews for all international transactions (31 C.F.R. Part V, Appendices A, B & C).

D. Adoption of Compliance Program

1. Communication from senior company officers regarding adoption of program.
2. Appointment of compliance administrator.
3. Preparation of compliance program policy documents.
4. Establishment of training and outreach activities.
5. Establishment of compliance telephone "hotline."
6. Establishment of audit function

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