

Creating and Maintaining an Export Controls Compliance Program

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Export Controls Quiz

- Question 1: If a US supplier or distributor does not export directly but instead sells and delivers a controlled product to a customer in Seattle, then the supplier or distributor is not subject to U.S. export controls
- Answer 1: False
- The supplier/distributor is still subject to US export controls as a “party” to the transfer of a controlled product
- A US-controlled product does not lose its control status simply by being handled inside the US (including Maintenance, Repair, Overhaul)
- Customer requirement
- Knew or should have known?

Export Controls Quiz

- Question 2: When a distributor sells a military part or assembly designed by an OEM, the OEM is solely liable for regulatory compliance for that part or assembly
- Answer 2: False
- Whether or not designed by the distributor, if distributor sells a part subject to the ITAR, distributor is also responsible for proper regulatory compliance for that part
- Exporter of Record?
- Knew or should have known?

Export Controls Quiz

- Question 3: For export control purposes, the control of the laser guided avionics of a Laser Guided Bomb is more important than its metal housing.
- Answer 3: It depends – all parts and components of a Laser Guided munition are subject to ITAR jurisdiction if they are “specially designed... for a military application”



Export Controls Quiz

- Question 4: A defense supplier or distributor registered with DDTC is required to name an “Empowered Official” who is solely responsible for our company’s compliance with the ITAR.
- Answer 4: False – Everyone at the company is potentially liable, especially its top management if they knew or should have known about a violation

Common Export Breakdowns

- Failure to determine jurisdiction and justify a rationale
- Technology released to foreign persons within the U.S. – “deemed exports”
- No control over server access
- Modification of commercial products for military uses



Common Export Breakdowns

- Appointment of an Empowered Official or Compliance Officer who is not truly empowered within the company
- **Suppliers and distributors who believe it's the OEM's problem**



Export Controls Enforcement

- Two U.S. agencies currently enforce export control regulations:
 - FBI and ICE



Export Controls Enforcement

- Mission of both agencies is the same:
 - Protect national security
 - Identify sensitive technologies and industries (i.e., aviation and defense)
 - Industry outreach
 - Inform industry of foreign threat and identify industry vulnerabilities
 - Investigate suspicious inquiries
 - Rivalry between agencies

Export Controls Enforcement

- Industry interviews by FBI and ICE:
 - Likely questions:
 - What is your commodity/technology?
 - Do you know its classification
 - How well do you know your customers?
 - Where do you sell it?
 - Transiting what locations?
 - Who are the intermediate consignees?
 - Who are the end users?
 - What's the end use?

Procurement Contract Audits



- Investigate suspicious exports or activities
- Enforcement Audits
 - In support of US Gov't procurement contracts
- Seizure of goods
- Arrest of individuals

DCAA

Dedicated to providing timely and responsive audits and financial advisory services

In Support of our National Defense

Penalties Under The EAR

- Penalties For EAR Violations:
 - Criminal (Entities): Up to US\$1 Million
 - Criminal (Individuals):
 - Up to US\$250,000/10 years prison
 - Civil Fines: US\$50,000
 - Denial of export privileges



Penalties Under The ITAR

- Penalties for ITAR Violations:
 - Criminal (Entities): Up to US\$1 Million
 - Criminal (Individuals):
 - Up to US\$1 Million/10 years prison
 - Civil Fines: Up to US\$500,000 and Forfeitures
 - Debarment from government contracts



Export Controls Enforcement

- 2007 ITT Corporation – US\$100 Million fine and 2 criminal convictions
 - Export of night vision tech to Singapore and Japan with knowledge of reexports to China
 - Started with domestic transfer of technology within US
 - Failure to track licensed exports due to be returned to the US
 - Incomplete or misleading information on license applications

Enforcement Against Parts Resellers

- April 5, 2012 - Alpine Aerospace Corp. and TS Trade Tech, Inc. of Closter N.J. agreed to suspended civil penalties of \$30,000 and \$20,000 respectively to settle 9 ITAR violations for missile parts exports to Korean Air Force
 - Resellers of low-cost engine parts
 - 6 exports of flywheel, latch, release mechanism, loader link and other parts

Enforcement Against Parts Resellers

- SED export number error claiming engine parts
- Failed to obtain a Non-transfer certificate
- Remedial compliance measures for 3 years, employee training, 2 external compliance audits of compliance program
- Without cooperation and remedial measures, fines could have been extreme

Aerospace Distributor prosecutions

- Aljaff Case - Feb 15, 2012
 - Mr. Aljaff, MVP Micro in CA sentenced to 30 months prison for sales of 13,000+ counterfeit integrated circuits (design and trademark infringements) to 420 US and foreign buyers (US Navy, aerospace among others, including distributors and others in the aerospace supply chain)
 - Value of US\$140,835
 - 20 import transactions
- Stephanie McCloskey Case – Vision Tech Components Administrative Manager
 - 38 Months in prison



Enforcement Against Individuals

- Jason Liang, owner of Sanwave Int'l sentenced April 23, 2012 to 4 years in prison and 3 years supervised release for exporting thermal imaging cameras to China without an export license.
 - Liang argued no damage to US national security, but violations are more like strict liability, not affected by resulting effect on national security
 - Recent lessening of licenses to 36 countries did not affect China

Export Management Compliance Programs – WHY?

- Reduces risk of export violations
- Smart business strategy
- Guidance to employees
 - Structure, organization, accountability
 - Consistency
 - Process
 - Training and awareness

Export Controls Compliance is Risk Management



Core Elements of an EMCP

1. Management Commitment
2. Continuous Risk Assessment
3. Formal, Written EMCP (policies and procedures)
4. Training
5. Cradle to Grave Compliance
6. Recordkeeping
7. Compliance Monitoring and Periodic Audits, including audits of business partners (upstream and downstream)
8. Procedure for Problems and Violations
9. Deciding Whether to Externally Disclose Violations

Why is an Export Management Compliance Program Necessary?



- EAR Supp 1 to Part 766 – An effective EMCP is a mitigating factor given great weight in any enforcement proceeding
- Consent Agreements and court orders reveal that BIS, OEE and DDTC, OC expect that all companies in the export chain have compliance programs
- Risk mitigation is smart business

1. Senior Management Commitment

- Top management must initiate and support compliance
- Management sets the company's "culture"
 - Condoning unethical or illegal activity creates a slippery slope
 - Foster an environment free from retribution
- Lead by example
- commit sufficient funding
- ensure appropriate senior organizational official(s) are responsible for compliance

2. Continuous Risk Assessment

- Anticipate, Assess, and Act
 - Anticipate - errors or intentional acts may and probably will happen
 - Assess – where and how within your organization might these happen?
 - Act – EMCP to mitigate risk
 - Develop policies and procedures before a problem arises
 - Identify roles and responsibilities

3. Formal, Written EMCP

- Written policy and procedures
- Map for compliance
- What to recognize
- Empowerment to question transactions
- Who to contact
- What to document
- Consistently applied throughout the organization

4. Training

- Effective employee training
 - Applicable regulations
 - Knowledge of company products/tech
 - Red flag transactions for your industry
 - Various training methods
 - Repeated and updated training
- Empowered Official and company commitment from all levels of management
- Internal recordkeeping and audit procedure

5. Cradle to Grave Compliance

- Security and Screening of employees, contractors, customers, products, and transactions
- Implementation of compliance safeguards throughout the export life cycle including product development, jurisdiction, classification, sales, license decisions, supply chain, servicing channels, and post-shipment activity

Cradle to Grave Compliance

- Large and small OEMs are increasingly auditing all stages of product supply & sales
 - Product development
 - Supply of parts and components
 - Deemed exports by suppliers
 - Marketing activities of distributors
 - Sales by distributors
 - DDTC registration of distributors?
 - EMCP by suppliers and distributors as a market advantage?

6. Recordkeeping

- Who - is obligated
- What - is to be retained
- Where - storage and security (physical and virtual)
 - Format for storage and reproduction
 - Requirement to produce records
 - OEMs are requiring upstream and downstream compliance
- When - retention period

Recordkeeping

- In 2005 ITAR recordkeeping requirements in §122.5 were clarified by DDTC:
 - Electronic records must be reproducible on paper and track all changes, author and date
 - §127.2 describes retention of “Any other document used in the regulation or control of a defense article, defense service, or technical data for which a license or approval is required by the ITAR”



Recordkeeping

- In combination with §123.22 regarding TAAs, companies are advised to retain records of all ITAR-related transactions of technical data, hardware, software, and services
- How long? – At least 5 years from the end of the export-related transaction or the expiration of an applicable license etc.
- EAR - see Part 762

7. Compliance Monitoring and Audits

- Conducted periodically, but not predictably
- Identify business units and personnel
- Record audit inquiries and results for tracking purposes
- Identify gaps and inconsistencies
- Written report to establish EMCP credibility
- Debrief all participants
 - Good results, problems, and lessons learned
- Recommendations
- Corrective measures

8. Procedure for Problems and Violations

- Reporting without reprisal
- Establish a clear procedure for reporting
- As determined by Company management, use neutral outside Legal Counsel not implicated in suspected export controls violations

Procedure for Problems and Violations

- To investigate and determine facts
- To recommend a course of action that weighs risks and benefits
- To recommend corrective action
- To Implement corrective action
- To interface with U.S. Government
- **Legal counsel as opposed to in-house counsel, consultant or accountant**
 - **To preserve confidentiality of communications**

9. Deciding Whether to Externally Disclose Violations

- Options regarding external disclosure of violations:
 - Do Nothing
 - Confidential internal corrective action without public disclosure
 - Voluntary Disclosure
 - The EAR §764.4-764.5 and ITAR §127.12 both encourage Voluntary Disclosures of violations
 - Voluntary Disclosure is a judgment call!

Deciding Whether to Externally Disclose Violations

- Disclosure of violation must be made prior to U.S. Government independently learning of the same or substantially similar information and commencing an investigation

- Goals of Disclosures
 - Mitigate liability
 - Narrow the investigation
 - Favorably interpret facts and regulations
 - Inform and guide U.S. agency investigators
 - Never lie; be trustworthy; seek a fair result
 - Show respect for law and U.S. Government's goals

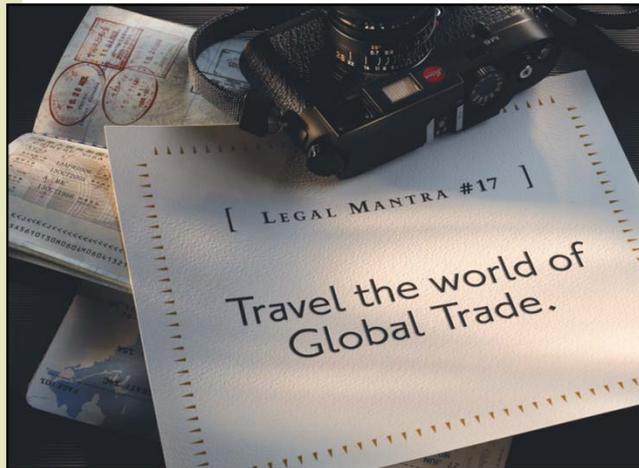
EMCP Summary Self-Audit

| TOPIC | Date Implemented | How Implemented | Date Operational | Personnel Involved | Dates Audited and/or Repeated |
|---|------------------|-----------------|------------------|--------------------|-------------------------------|
| 1. Management Commitment | | | | | |
| 2. Continuous Risk Assessment | | | | | |
| 3. Formal, Written EMCP | | | | | |
| 4. Training | | | | | |
| 5. Cradle to Grave Compliance | | | | | |
| 6. Recordkeeping | | | | | |
| 7. Compliance Monitoring and Audits | | | | | |
| 8. Procedure for Problems and Violations | | | | | |
| 9. Deciding Whether to Externally Disclose Violations | | | | | |

Why Comply?

- Protection of National Security Goals (as defined by the U.S. Government)
- “An ounce of prevention is worth a pound of cure”
- It’s the law....

Thank You.



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