

Export Controls and International Sanctions Compliance

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The case of Mr. G.

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Mr. G. was the shipping manager for a US company manufacturing and supplying certain electronic products. Some products of this company are subject to export controls and need a license for export.

The company became aware that Mr. G. had committed violations of export control regulations and, therefore, the company submitted a voluntary self-disclosure to the Department of Commerce's Office of Export Enforcement.

Mr. G. admitted having violated the law, but claimed that the company did not devote sufficient resources to ensure compliance and that he had to give priority to other tasks.

Mr. G. was sentenced to 42 months in prison and USD 1,000 fine.

The company was fined USD 500,000 by the US District Court for Pennsylvania due to inadequate management of export controls risks.

Overview

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- Export controls and sanctions as a part of various trade compliance areas
- Framework of rules on trade of goods, software, technology, economic resources
- Instruments: Restrictions on movement and/or use, licensing requirements, administrative obligations, as well as financial restrictions – all of which take precedence over any contractual arrangements
- Targets: countries or persons (sanctions) or specific goods (export controls)
- Reasons:
 1. Non-proliferation
 2. Prevention of uncontrolled transfers of conventional military arms, military goods and dual goods and technologies
 3. Combating terrorism and other violations of international law (trade restrictions)

Why trade compliance?

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Legal and political requirements

- Political issues and increasing and expanding legislation

Protecting executives and employees against

- Custodial sentences and other penalties (in CH: Sanctions: up to 5 years and up to CHF 1m; Export Controls: up to 10 years and up to CHF 5m*; in the US up to 20 years)

* No SECO statistics; see published decisions of Swiss Federal Supreme Court, Swiss Criminal Federal Court as well as media reports.

Preventing damages

- Civil liability
- Fines
- Revoked / denied licenses
- Frozen / blocked funds
- Seizure / forfeiture of goods
- Reputation

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Export controls

Regulations and authorities

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Switzerland	Güterkontrollgesetz (GKG), Güterkontrollverordnung (GKV), Chemikalienkontrollverordnung (ChKV) Kriegsmaterialgesetz (KMG), Kriegsmaterialverordnung (KMV),	State Secretariat for Economic Affairs (SECO) (appeal to federal jurisdiction)
EU	Regulation (EC) No 428/2009, annex Member states regulations	Member states' authorities respectively
US	<i>Commerce Control List</i> (to identify goods subject to export controls) in connection with <i>Country Chart Part 738 of EAR</i> (to see whether or not a license is required based on ECCN "Reason for Control")	Buro of Industry and Security (BIS)
<i>International good control regimes and treaties: Australia Group, Nuclear Supplier Group, Missile Technology Control Regime, Wassenaar Arrangement, Chemical Weapons Treaty, Biological Weapons Treaty, Nuclear Weapons Non-Proliferation Treaty, Arms Trade Treat</i>		

What is export controlled?

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Controlled items:

- **Military items** (incl. goods specially designed or subsequently modified for such purposes) and **Dual use items** (i.e. goods on control lists which can be used for civilian and military ends), outlined in national lists
- **Any other (not listed) items** if it is known or the circumstances give reason to suspect that they are intended to be used for an end-use related to weapons of mass destruction (**Catch-all rule**)

This includes

- **goods**,
- **software** and
- **technology** related thereto (e.g. specifications, drawings)

Applicability

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Any export (or transit and brokerage) by

- **physical transfer**
- **intangible transfer** e.g. by email, fax, download from company intranet
- “deemed export” (US)

Applicable regulations

- of the country **from which a product is physically/intangibly exported**
- of the **country of origin** in some cases of re-exports (extraterritoriality)
(e.g. US law as soon as US origin content of the product exceeds 10% or 25% of the re-sale price – “De-minimis rule”)

Responsibility

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Responsibility

- “Exporter” – generally manufacturer/dealer, i.e. company with title and control over the good at the time of the export
- Other service providers (freight forwarder, carrier, customs declarant, insurance, bank) – for complicity, in case

(s. also BStGer 30.5.2017 SK.2016.51)

Example: Swiss good export control

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General export license for dual use goods into certain countries or **individual** export license for dual goods in other cases:

- a) Exporter in Switzerland (GKV 5 I)
- b) Proof of reliable internal controls on compliance (GKV 5 II / 11)
- c) No concrete indications of an illegal use, e.g. in case of proliferation, regional tension and instability, goods not staying with the declared end-customer, export refusal by a partner country, ensuring re-export controls requests, destination country's import prohibition (GKV 6)
- d) Documentation (e.g. company profile, transaction documents, import certificate only upon request, statement of end use)

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International sanctions

Regulations and authorities

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Switzerland	Embargogesetz (EmbG) Based thereon: Ordinances on sanctions	State Secretariat for Economic Affairs (SECO) (appeal to federal jurisdiction)
EU	EU restrictive measures decided by the EU Council following the EU Common Foreign and Security Policy	Member states' authorities respectively
US	Various country and person/entity based sanctions	US Department of Treasury / Office of Foreign Assets Control (OFAC)

Applicability

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- Irrespective of whether exports or domestic activities/dealings
 - CH: Crimes committed in Switzerland (**territoriality** principle)
 - EU: Crimes committed in the EU (**territoriality** principle) or by EU citizens (**personality** principle/**extraterritoriality**)
 - US: Crimes committed by US persons (companies, citizens, resident aliens, any persons while in the US) inside or outside the US (**personality** principle/**extraterritoriality**)
- Need to comply with all applicable rules irrespective of territoriality principle (e.g. lawful transaction in CH under CH-law, but US-employee would breach US-law).

Categories

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- *Country based*
- *Person and entity based*

- *International*, e.g. UN or OSCE sanctions
 - Switzerland, as UN member, must adopt the UN sanctions (Art. 25 UN Charta)
- *Unilateral*, e.g. many US sanctions; certain EU sanctions against Iran, Russia, etc.
 - Switzerland increasingly aligns its sanctions with the EU sanctions, although there is no legal obligation; No alignment with US sanctions

Country based sanctions

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- *Comprehensive* (e.g. US OFAC sanctions against Iran, Cuba, N. Korea, Syria) → Virtually all business, exports, re-exports prohibited
- *“Smart sanctions”*, i.e. targeted against specific persons and entities or restricting trade with key commodities, e.g.
 - freezing of funds,
 - ban on transactions,
 - license requirements and investment restrictions,
 - trade restrictions on certain goods/services,
 - travel restrictions,
 - diplomatic constraints,
 - air traffic restrictions, etc.

Person and entity based sanctions

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Person and entity based (international lists of restricted parties), e.g.

- EU and CH sanctions against “Designated Persons”
- US sanctions against (a) specially designated nationals (“SDNs”), (b) terrorists, (c) narcotics traffickers, (d) WMD proliferators, (e) transnational criminal organizations

Instruments:

- (a) **Freezing** of funds and economic resources belonging to, owned, held or controlled by sanctioned parties
- (b) **Prohibitions on making** funds or economic resources **available**, directly or indirectly, to or for the benefit of sanctioned parties. → Risk of **indirect dealings**: prohibited relationships may include subsidiary, shareholder (EU: majority in votes, shares or other influence), director, contractor, family member

→ Required **review of the lists** and **screening of the partners**

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Application Examples

- (1) Laurent is French, works for a Swiss company with operations in China and USA. Is he subject to EU trade sanctions?
- (2) Hans Peter is Swiss and German citizen. He works for an affiliate of a Swiss company in Shanghai. He travels from China to Iran on business and wants to bring his drawings of a CNC machine saved on his laptop. Are the data subject to CH/EU export controls?
- (3) Controls on dual use products are concerned with the export of goods, software and technology by any means, but not transfers between companies that are part of the same corporate group. Right?
- (4) Pascal is a Swiss citizen and is going to travel on business to India with a USB stick, containing technical drawings regarding controlled machines of its company. He will not distribute the drawings, but just refer to them personally. Is he concerned by CH export controls?

- (5) Bernhard is in India at a supplier's site and access the technical drawings of a 5 axis milling machine (export controlled) from the company's sharepoint. Is this subject to export controls?
- (6) If you determine that your product is neither military nor dual use, is no license required? And if the product is a used machine?
- (7) You sell a non-controlled item with potential prohibited end-uses. You have however previously obtained a license for the same product to a different destination and a license for a similar product. Can you avoid to request a license?
- (8) A Spanish subsidiary has the opportunity to sell a machine to a customer in Cuba, which is subject to comprehensive US sanctions. Because the value of the contract exceeds a certain amount, approval has to be obtained by the head of the business unit who is a US citizen living in Switzerland. Can he approve?

- (9) The above transaction has been consummated. For after sales services, the Spanish subsidiary asks the US affiliate to send an employee from Miami in order to limit the costs. Can the employee go?
- (10) A potential customer is a designated party under international sanctions. Can you (a) contact him by letter, email, phone? (b) offer him goods and services? (c) supply to him software and technology? (d) return to him a down-payment due to difficulties of the business?

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How to deal with these issues?

Internal control program

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Adequate organizational measures to prevent breaches of law

→ effectivity of controls, efficiency, prevention of damages/liability, ensuring evidence

1. Management commitment and policy statement
2. Risk analysis
3. Organization, responsibilities, resources
4. Processes – “know your product” / “know your customer” related
5. Trainings and information
6. Controls and corrections

Management commitment, policy statement

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- **Commitment** (e.g. in Code of Conduct)
- “Tone at the top”
- **Manager** responsible for exports / Responsibility for ICP implementation
- Mechanisms for **upwards reporting** and **escalation process**

Risk analysis

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- **Identification and assessment** of compliance risks
- **Criteria:** e.g.
 - Kind of products and export goods' classification (e.g. are goods and services subject to sanctions/controls? highly precise machines, chemicals resistant pipes?)
 - Company's business activities and customer portfolio (e.g. close to military?)
 - Territory (e.g. place of origin, destination, transition, place of subsidiaries and intermediaries)
 - Distribution method (directly to end-customer, through intermediaries, etc.?)
 - Counterparty (client, agent, freight forwarder, bank)
 - Currency of the deals (USD leads to US sanctions exposure)
 - Company's dimension, structure, organization etc.
 - Relationship with authorities
- **Ongoing review** of legal changes, applicability of export controls and sanctions, products, customers, activities etc.

Organization and responsibilities

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- Organizational chart (with reporting lines) accessible to all – Example of functions:
 - **Top manager** responsible for exports
 - **CCO**
 - **Local management** for execution / ensuring adherence to law
 - **Local export controls appointees** for assessing and identifying risks, advising local management, ensuring compliance, keeping abreast of requirements and legal developments, reporting risks and suspicious cases, etc.)
 - **Technical engineers** for item classification
 - **Logistics and procurement** for suppliers' information (e.g. controlled US parts)
 - **Sales** for control of intermediaries (e.g. contractual obligations) and screening
- Export controls manager must be able to stop or release an export and report directly to the top management
- Sufficient human, technical (IT) and other resources (acc. to risk analysis)

Processes

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- **Directive** defining
 - Objectives and basic principles (e.g. due diligence and investigation of suspect cases, screening, no deal in suspicious cases, no circumvention, legal advise)
 - Procedures:
 - Item classification
 - Export process from order receipt to shipping
 - Licensing process
 - Interaction among departments
 - Interaction with authorities (e.g. notification of suspicious orders)
 - Due diligence and screening process re end-customers, receiver of resources; red flags (examples) etc.
 - Reporting
 - Responsibilities
 - Documentation

Processes / Export questions

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- **Where to? (sanctioned territories?)**

Do any sanctions apply to the specific export?

Is the destination country used for onward supply to sanctioned countries?

- **What is my item? (products controlled?)**

Is it export controlled in the export country (in lists)?

Does it contain any US controlled component? If so, with value of >10% or 25% of the total price? → Ask supplier and get written confirmation

- **What for? (sensitive end use?)**

Never export for prohibited end-uses and watch for red flags

- **To whom and who is involved? (sanctioned parties?)**

Know your customer and watch for red flags

What is my item?

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Export classification

- **Switzerland:** *Güterkontrollgesetz, annexes 1 and 2*
- **EU:** *Regulation (EC) No 428/2009, annex 1*
- **USA:** *Commerce Control List - CCL (to identify items subject to export controls) in connection with Country Chart Part 738 of EAR (to see whether or not a license is required based on ECCN “Reason for Control”)*
- **China:** *Catalogue of Dual-Use Items and Technologies Subject to Import & Export License Administration*

All relevant commercial documents for goods under export license must clearly indicate that the items are subject to export controls if exported ([declaration on products, packaging, invoices and delivery papers](#)).

What for and to whom? Due diligence

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- **Know your customer and watch for red flags** (Do you really know your customer, its background and its typical business? Does it know its customer? What is the end-use of your product? Will your customer “use” or resell your product? Are you sure your customer/end-user is not on one of the restricted end-users/uses lists? Who is the exporter/re-exporter of record?)
- **Screening** of business partners, third parties (agents, distributors, agents, freight forwarders, banks etc.) and related persons (in particular in sensitive countries also directors and shareholders) against information in your possess: You should at least know what the authorities know from public sources. Advisable use of IT tools.
- **Risk based approach** for more problematic territories / due diligence accordingly. In suspect cases, **investigate further and ascertain the facts to a reasonable extent**.
- **Document** (a) standard screening process as well as (b) individual screening analysis and the investigation measures.

Further security measures

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- Protection of the company through compliance language in contracts, e.g.
 - providing intermediary/reseller with **information on your company's policy**,
 - including a **clause into agreements** with resellers re (1) obligation to comply with export control regulations and sanctions and (2) your company's right to give notice of termination in case of violation,
 - entering into an overall **compliance agreement**.
- **Prevent any involvement** of persons who may be subject to fines etc. (e.g. "US persons") if your dealing is otherwise legally allowed under your jurisdiction.

No circumvention

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- If it is suspected that the products to be exported are likely to be misused, the **contemplated transaction will not be carried out.**
- Any **evasion of export restrictions is forbidden**, e.g.
 - making shipments via domestic or foreign dealers or other intermediaries
 - splitting order into smaller orders falling below statutory thresholds
 - keeping end-user statements unclear, incomplete or even false
 - ignoring a likely misuse of the product for illegal purposes

Thanks for your attention!

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Questions?