

U.S. Export Control Laws

**Holland & Hart
International Practice Group
Trip Mackintosh**

July 31, 2001

I. General overview.

U.S. export control laws apply to virtually every international transaction. In most cases, the controls permit the transaction under a general license or through broad regulatory exemptions. In certain instances, however, federal regulations create specific obligations and impose significant penalties for violations.

Federal regulations restrict with whom a U.S. person can do business, how that business is done and what may be transferred. Everything from financial transactions, dealership agreements, distribution arrangements, stock transfers, exports of know-how, technology transfers, to mere proposals for certain exports are caught in this regulatory regime. The general rule to follow is that if the transaction involves international commerce, federal controls likely apply.

II. Why this area of law is important.

The majority of U.S. companies of any size have an international aspect to their operations. Stockbrokers, banks, and real estate companies may all have non-U.S. investors or clients. Manufacturing or service firms may have clients or operations outside of the United States. Natural resource companies may have non-U.S. operations, investors, partners or customers.

The internet has increased the likelihood that most U.S. companies will face international regulatory issues. The market is now global and growing. With the electronic superhighway, marketing is ubiquitous, as potential customers from Baghdad to Buffalo have equal access to a company's web page.

Without an appreciation of U.S. export controls, a U.S. business risks inadvertent violations with significant consequences because problems can occur in unlikely circumstances. For example, a franchise agreement between a U.S. real estate company and a South African partnership may violate U.S. Treasury Department sanctions, due to the nationality of investors in the South African entity. A minerals contract drafted for U.S. and Canadian companies similarly could violate Treasury Department controls on Cuban assets. Negotiating a joint venture with non-U.S. investment partners could result in an unintended illegal export of controlled technology. Employing non-U.S.

labor -- within the United States -- could result in illegal “deemed” exports of controlled technology.

III. When these laws are likely to impact a U.S. business.

If a U.S. company conducts business with a non-U.S. person, the U.S. company needs to anticipate the impact of U.S. export control laws. As the laws may restrict with whom business can be conducted and what can be sold, promotional materials should indicate as much, so as to lessen the impact of the regulatory restrictions on the potential customer as the transaction matures.

Export controls on technology generally apply regardless of the location of the “U.S.-origin technology.” For example, a subsidiary of a U.S. company that is selling “U.S.-origin technology” in eastern Europe is subject to these controls, as if it were making sales from the United States. This subsidiary can comply fully with the laws of the country where it is located and still create liability for the parent company under U.S. law.

With regard to joint ventures, the direct product of U.S.-origin technology also is controlled for export purposes (with some exceptions). This means that if a U.S. firm transfers manufacturing know-how to a partner in Mexico, U.S. law might govern the sale of the direct products of this technology -- even if made in Mexico -- as if the product had been manufactured in the United States.

IV. Overview of export control laws.

a. With Whom You Can Trade.

i. Treasury Department Embargoes.

By virtue of the Trading with the Enemy Act, the International Economic Emergency Powers Act (“IEEPA”), and several other laws directed at specific countries, the U.S. Treasury Department prohibits or restricts trade with a list of countries and an ever-growing directory of individuals and companies. The Treasury Department’s Office of Foreign Assets Control (“OFAC”) is charged with writing and enforcing the regulations. *See generally* 31 C.F.R. §§ 500, *et seq.*

These regulations can vary from country to country with little apparent logic. For example, certain oil field development equipment can be exported to Iraq; but not to Iran. Travel is permitted to Iran; but a U.S. citizen going to Cuba can face severe fines. In addition, political developments may put reality ahead of the regulations, leaving U.S. businesses in a state of confusion. As a case in point, when the United States improved its relations with the former Yugoslavia and promised aid and investment, Treasury’s rules remained unchanged, prohibiting most trade and threatening severe penalties for violators.

It is often impossible to predict which of a company's international customers might create potential problems under these embargo regulations. When the U.S. government determines that a party is a buyer for an embargoed country, the U.S. government "specially designates" this party as a national of that country. Inclusion on this list can occur at any time, even during the pendency of a transaction with a U.S. company. Once a party is put on a prohibited parties list, it joins drug traffickers and terrorists with which no commerce, no commercial transaction of any sort is permitted.

The consequence of these regulations is that **prior to initiating** a transaction with a non-U.S. national or permanent resident, a U.S. company must consult the Treasury Department lists. The prohibited transactions include almost all commercial activity, including services such as banking, stock brokerage, real estate, etc.

The Treasury Department regulations also prohibit indirect transactions, such as those done through various corporate forms or contractual arrangements. Simply put, U.S. parties cannot deal with intermediaries to conclude otherwise prohibited transactions.

If violations are suspected, the U.S. government can stop a transaction and seize the technology, vessel, etc., **if even one** of the parties to the transaction is suspected of violating these laws. Therefore, the soundness of an international transaction is only as good as the compliance of all its participants.

Laws of other countries often create conflicts on these issues. For example, a Mexican joint venture partner who legally can trade with Cuba might produce liability for its U.S. partner by continuing such business. Further, no other country has the breadth of controls imposed by the United States. This means that non-U.S. partners may be impatient with U.S. regulatory requirements, making violations more likely.

ii. Commerce Department Denied Persons List.

Just as the Treasury Department prohibits **all** trade with certain parties, the Commerce Department prohibits **any assistance with an export transaction** involving parties determined to have violated U.S. export control laws. This prohibits financing, services of any sort, shipping, management functions, etc. that could assist with an export transaction. *See generally* Export Administration Regulations ("EARs"), 15 C.F.R. §§ 730, *et seq.* Again, **prior to initiating** a transaction, a U.S. company has to ensure that the other party is not on the Commerce Department Denied Persons List.

iii. State Department Debarred Parties.

The State Department maintains a list of "debarred" parties who are prohibited from participating in any transaction in which a State Department licensee is involved. The State Department regulates the export and (some) imports of munitions and technologies that are specifically designed or modified for military use. As with the

Commerce list, parties are put on the “debarred” list for a limited period of time, usually less than three years.

iv. Commerce Department “Entities List.”

The Commerce Department also introduced the “entities list” several years ago. This list enumerates those entities (including individuals) that have been engaged in the proliferation of weapons of mass destruction, missile technology, biological and chemical weapons, etc. No U.S. technology can be exported to these parties without a license. License applications are generally denied.

b. What Can be Sold.

i. Commerce Department Bureau of Export Administration.

The Export Administration Act and its implementing regulations, the EARs, control most exports. The vast majority of exports are permissible under a general license or general exception to the controls. High-end technology and related services, however, risk falling into a controlled category given their potential military use.

ii. State Department Controls.

The State Department governs exports and (some) imports of “munitions,” as defined by the Arms Export Control Act and the International Traffic in Arms Regulations. “Munitions” is read broadly to include more than conventional notions of arms. The category includes virtually all other technology that has been “specifically designed or modified for military use.” Further, the State Department has the ability to designate a technology as a “munition,” if in its opinion national security concerns warrant the control.

iii. Commerce and State Department Overlap.

This often overlapping export control jurisdiction between Commerce and State confuses exporters. Frequently, exporters assume a product is controlled for export by State (due to its military application), when Commerce controls the item, and vice versa. Errors in this area, however, can be costly, as penalties are significant.

iv. Department of Energy

Within the Department of Energy, the Nuclear Regulatory Commission (“NRC”) controls the export of technology used in certain aspects of nuclear power generation. The scope of NRC controls is significantly less than those of Commerce or State, but may impact energy or consulting firms in the United States.

c. Conditions of Sale/Anti-Boycott Regulations.

The Commerce export rules also prohibit supporting another country's boycott of a nation that is friendly to the United States. Under most administrations, this control is aimed only at the Arab League boycott of Israel. Occasionally, however, other bilateral boycotts are caught in these controls, as foreign policy initiatives vary.

For U.S. companies, these regulations present compliance and reporting challenges. The regulations not only prevent supporting the boycott; but they require reporting to Commerce of any "invitation" to support the boycott (*e.g.*, letter of credit term) that is declined by the U.S. company. Often, the "invitations" are subtle to a degree that unless the company's representative is well trained, mistakes can occur.

V. Enforcement considerations .

Knowing violations of the Treasury regulations can produce fines of \$1,000,000 (for a corporation) and \$100,000 (for an individual) or up to ten years in prison for violations of the Cuban sanctions. Civil penalties can range to \$55,000 per violation. For other embargoes (*e.g.*, the Iranian sanctions), penalties are less. Civil penalties range to \$11,000 per violation; with criminal penalties carrying a fine of \$55,000 or ten years in prison.

Export violations under the Commerce rules can result in civil penalties of up to \$100,000 and/or denial of export privileges. Also possible are criminal sanctions of up to ten years in prison and/or fines of five times the value of the export or \$1,000,000 (for a corporation) and \$250,000 (for an individual).

The State Department can impose fines of \$1,000,000 or ten years imprisonment for willful violations of its rules; civil violations can result in penalties up to \$500,000. In addition, the State Department can "debar" a violator, making the person or entity ineligible to receive export of State Department licensed technology or participate in contracts involving such technology.

Penalties under the NRC export rules can result in criminal fines ranging up to 20 years imprisonment and \$20,000 per violation.

Importantly, under all of these regulatory regimes, each export can produce multiple violations. The penalties are not per "transaction," leaving open the possibility that one export transaction can produce multiple violations and rapidly increase an exporter's liability.

VI. Compliance.

The array of possible penalties (including denial of export privileges) means that most exporters have an interest in effective compliance programs and an ability to

respond proactively to perceived violations. Often, with compliance efforts and proactive representation, the exporter can work with the regulatory agency to minimize the impact of the violation.

Compliance begins with the sales materials or initial contacts. At this point in the transaction, parties have to be screened to be sure business is allowed and the potential exporter needs to determine if the technology sought by the non-U.S. party can go to the intended destination.

Holland & Hart has extensive experience in developing these compliance programs. As part of our effort to refine these programs, we are currently exploring the creation of client-specific internet-based training and compliance modules for this complex area of law.

VII. Further information.

The International Practice Group hopes this outline has been useful. If you require additional information or if you have questions of any sort, please let me know. I am in the Denver office at 303-295-8186. Kevin Johnson, head of the International Practice Group is also in Denver, at 303-295-8486.

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