Export Compliance for Freight Forwarders

International Freight Forwarders and Customs House Brokers Association of Atlanta

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Seminar Overview

- Recent Developments
- Overview of EAR
- Overview of OFAC Regulations
- Overview of ITAR
- Overview of Census Regulations
- Approaches to Export Compliance for Freight Companies
Recent Developments: Higher Penalties

- Increased penalties for many export violations
  - Civil penalties *per violation* of up to $250,000 or twice the amount of the transaction that is the basis of the violation, whichever is greater (raised May 22, 2006 from $11,000 to $50,000 and then again on October 16, 2007 to $250,000)
  - ITAR civil penalties of $500,000 per violation
  - Criminal fines up to $1,000,000 per violation; imprisonment up to 20 years
  - Debarment
Recent Developments: More Cases

- Increased enforcement of export violations
  - OEE, FBI and ICE all cooperate under Department of Justice's Export Enforcement Initiative
  - DOJ's newly established National Security Division is training more federal prosecutors across the country to handle export controls prosecutions
  - “Counter-Proliferation Task Forces” are being formed in all USAOs
- More criminal prosecutions
- More investigations and inquiries
Recent Developments (Transportation Providers)

- Trend towards pursuing third parties, such as forwarders and transportation companies
- Agencies view these parties as a “last line of defense”
- Agencies see need to focus on forwarder compliance because exporters are “outsourcing’ compliance to forwarders
- Forwarders and transportation companies targeted for enforcement and audits and compliance checks
Transportation Provider Penalty Examples

- Eastways Shipping Corp.: $70k civil penalty for making shipments of scrap metal to party on BIS Entity List
- Elite International Transportation: $156k penalty for putting NLR on SED when materials being shipped required an export license
- DSV Samson Transport: $649k in criminal and civil penalties for making shipments to party on BIS Entity List
- About 2/3rds of penalty cases against forwarders are related to exports to prohibited persons or places
DHL Case

- August 2009-- DHL settles OFAC and BIS charges of aiding and abetting exports of goods to Syria, Sudan and Iran and failing to maintain records-- $9.44M PENALTY AND 2+ YEAR AUDIT REQUIREMENT

- DHL failed to retain air waybills and other export documents– wide range of shipment records must be retained for 5 years

- Records were missing for thousands of shipments

- Fewer than 100 shipments to/from Iran, Syria and Sudan were specifically charged
Export Controls Overview

- Controls on “items” or “articles” – products, technology & software-- & defense services
- Controls on “end uses” – non-proliferation
- Controls on exports to embargoed countries
- Controls on exports to “end users”
- Prohibitions on facilitating, causing, inducing, permitting, and aiding and abetting violations of export laws
- Multiple agency regulations (and penalties)
Overview of EAR
Overview of EAR

- The EAR is administered by BIS
- The primary focus of export controls under the EAR is to control the export of “dual use” (i.e., products capable of either military or non-military use)
- The EAR may allow, prohibit, or require licenses for certain export transactions
- The term “dual use” is often misleading, as it encompasses products that have no appreciable military application
- Generally, any item that is not designed specifically for military use will be regulated by the EAR
Scope of EAR

- EAR govern export and reexport of:
  - US origin items and items in US
  - Foreign manufactured goods containing US origin parts or materials in excess of *de minimis*
  - Foreign made direct products of US technology or software
  - The release of technology overseas or to foreign nationals in US (deemed export rule)
Exports and Re-exports

- An export is from the United States to the ultimate destination
  - Beware of transshipments
- A re-export is the shipment or transmission of items from one foreign country to another foreign country
- Thus, items in some foreign export transactions are subject to the EAR
Prohibited end uses for exports include use in the design, development, production or use of:
- Certain nuclear activities
- Certain missiles, rockets and UAVs
- Certain chemical and biological weapons
- Maritime nuclear propulsion
- Only applicable to certain countries
- New rule restricts military end use in China
May not export goods to prohibited end users, including:

- Denied persons
- Persons on Entity List or other non-proliferation lists
- Debarred persons

Common enforcement area, especially for transportation providers
EAR Item-based controls

- **EAR – “Dual use” Items**
  - Listed items – on Commerce Control List (CCL) (Supp. No. 1 to Part 774 of EARs)
  - Classification of goods and technology in Categories 0 through 9 (e.g., Materials, chemicals, microorganisms and toxins (1), Electronics (3), Computers (4), Telecommunications and Information Security (5))
  - Unlisted items – EAR99
  - Multilateral Wassenaar Arrangement
  - Classification, country of destination, and applicability of license exceptions determine controls
EAR- Routed Export Transactions

- Foreign PPI takes express written responsibility for export licensing requirements and assuring export authorization from USPPI
- Foreign PPI issues POA to US agent, i.e., the foreign party’s freight forwarder to handle export requirements
- In such cases, the freight forwarder is the “exporter” and is responsible for determining export licensing requirements
- Similar, but slightly different concept of routed transactions under Census regulations– EXERCISE EXTRA CAUTION WHEN SERVING AS AGENT TO FPPI.
Red Flags

- De facto “Know Your Customer” rule for exports requiring attention to Red Flags (EAR Supplement No. 3 to Part 732)
- No Self-Blinding
- Routine installation, training or maintenance services are declined by the customer
- Delivery dates are vague, or deliveries are planned for out-of-the-way destinations
- A freight forwarding firm is listed as the product's final destination
- The shipping route is abnormal for the product and destination
- Packaging is inconsistent with the stated method of shipment or destination
- When questioned, the buyer is evasive or unclear about whether the purchased product is for domestic use, export or re-export
Red Flags (Continued)

 The customer or purchasing agent is reluctant to offer information about the end-use of a product
 The product's capabilities do not fit the buyer's line of business
 The product ordered is incompatible with the technical level of the country to which the product is being shipped
 The customer has little or no business background
 The customer is willing to pay cash for a very expensive item when the terms of the sale call for financing
 The customer is unfamiliar with the product's performance characteristics but still wants the product
 Resolve Red Flags or do NOT ship
The EAR requires the following records to be maintained for each export shipment by any person (including forwarder) when records are made or obtained by that person:

- Export control documents (e.g., B/L’s, air waybills, commercial invoices, packing lists)
- Purchase Orders
- Memoranda
- Notes
- Correspondence
- Contracts
- Invitations to bid
- Books of accounts
- Financial records
- Restrictive trade practices or boycott documents and reports
Example Prohibitions under EAR

- Engage in conduct prohibited by EAR
- Cause or aid, abet, counsel, command, induce, procure or permit the doing of any act prohibited by the EAR
- Remove, conceal, store, dispose of, transfer, transport, forward, or otherwise service, in whole or in part, any item exported or to be exported from the United States with knowledge that a violation of the EAR has occurred or will occur.
- Fail to comply with recordkeeping requirements.
Overview of OFAC Regulations
Overview of OFAC

- Two main statutory bases for US sanctions:
  - Trading with the Enemy Act (1917)
    - Older programs are under TWEA, all rest under IEEPA
    - Both have jurisdictional predicates of persons or property subject to US jurisdiction
    - TWEA-based programs define US person to include controlled foreign subsidiaries of US persons. IEEPA ones do not
- Multilateral sanctions
- Unilateral US sanctions
Overview of OFAC Sanctions

- Each program is different
- Typically block assets and prohibit transactions
- Apply to all persons subject to the jurisdiction of the US, including, in some cases, foreign subsidiaries and affiliates of US companies
- US persons and covered companies prohibited from dealing directly or indirectly with targets
- Expansive concepts of prohibited “export of services” and “facilitation”
- Broad anti-evasion provisions
Types of Restrictions

- OFAC administers and enforces economic and trade sanctions against specified:
  - Foreign governments (e.g., Iran, Sudan, Cuba)
  - Individuals (e.g., terrorists, narcotics traffickers)
  - Entities (e.g., drug front companies, charities linked to terrorist groups)
  - Practices (e.g., trade in non-certified rough diamonds)
Scope of OFAC Restrictions

- Generally OFAC restrictions apply to activities of all US persons.
- In most OFAC programs, “U.S. person” is broadly defined as:
  - Any U.S. citizen
  - Permanent resident alien
  - Entity organized under the laws of the United States (including foreign branches)
  - Any person in the United States
- Some regulations, including those that cover Cuba, extend further to include foreign entities that are owned or controlled by U.S. individuals or entities.
Current Sanctions

- 30 sanctions programs (country-based, list-based, counterterrorism, narcotics)
- Full-scope embargoes:
  - Cuba (31 CFR Part 515)
  - Iran (31 CFR Part 560)
  - Sudan (31 CFR Part 558)
- Recently lifted/modified full-scope embargoes:
  - Iraq (31 CFR Part 575)
  - Libya (31 CFR Part 550)
  - Palestinian Authority (July 17, 2006)
- Partial and/or list-based sanctions:
  - Burma (31 CFR Part 537)
  - Former Liberian Regime of Charles Taylor (31 CFR Part 593)
  - Syria (E.O. 13338 (May 11, 2004); 31 CFR Part 542)
  - Zimbabwe (31 CFR Part 541)
  - Belarus (E.O. 13405 (June 19, 2006)
  - Cote d’Ivoire (E.O. 13396) (February 8, 2006)
  - Hamas (31 CFR Part 595 designation on April 12, 2006)
  - Democratic Republic of Congo (E.O. 13413) (October 27, 2006)
  - Lebanon (E.O. 13441) (August 3, 2007)
- Residual sanctions:
  - Balkans (31 CFR Part 588)
  - North Korea (31 CFR Part 500)
Sanctioned Entities and Individuals

- Four sets of anti-terrorism regulations:
  - Global Terrorism Sanctions Regulations (31 CFR Part 594)
  - Terrorism Sanctions Regulations (31 CFR Part 595)
  - Terrorism List Governments Sanctions Regulations (31 CFR Part 596)
  - Foreign Terrorist Organizations Sanctions Regulations (31 CFR Part 536)
Sanctioned Entities and Individuals (cont’d)

- Narcotics Trafficking Sanctions Regulations (31 CFR Part 536)
- Foreign Narcotics Kingpin Sanctions Regulations (31 CFR Part 598)
- Weapons of Mass Destruction Trade Control Regulations (31 CFR Part 539)
- Highly Enriched Uranium Assets Control Regulations (31 CFR Part 540)
Specially Designated Nationals ("SDN" List)

- The “Bad Guys” List-- Available at: www.treas.gov/offices/enforcement/ofac/sdn/t11sdn.pdf
- Example: BIN LADEN, Osama (a.k.a. BIN LADEN, Usama; a.k.a. BIN LADIN, Osama; a.k.a. BIN LADIN, Osama bin Muhammad bin Awad; a.k.a. BIN LADIN, Usama; a.k.a. BIN LADIN, Usama bin Muhammad bin Awad); DOB 30 Jul 57; alt. DOB 1958; POB Jeddah, Saudi Arabia; alt. POB Yemen (individual) [SDT] [SDGT]
Examples of OFAC Prohibitions

- Prohibition on the “…the exportation, reexportation, sale, or supply, directly or indirectly, from the United States, or by a United States person, wherever located, of any goods, technology, or services to Iran”
- Includes exportation and reexportation to a person in a third country undertaken with knowledge or “reason to know” the export is:
  - Intended specifically for supply, directly or indirectly, to Iran
  - Intended specifically for incorporation into goods to be supplied to Iran
- Prohibition on the facilitation by a US person, of the exportation or reexportation of goods, technology or services from Sudan to any destination or to Sudan from any location
OFAC Compliance Audits

- OFAC has a freight forwarder audit program
- Companies selected based on “risk profile,” including areas of world served
- Focus on small forwarders
- Advance notice provided
- Typically half to full day exercise
- Look for Senior mgt and compliance personnel involvement in audit
- Look for written compliance program, designated compliance personnel, training, internal auditing, management support
- Examine screening measures in place
OFAC Audits- Records

- Review documents to ensure retention
- Transportation Documents-
  - Bill of lading and documents reflecting all consignees, notify parties, forwarding agents, ports of loading and discharge and transshipment, destination, vessels and carriers
- Commercial Invoices reflecting sellers buyers, agents, manufacturers, Incoterms
- Certificates of Origin, transport details
Overview of ITAR
Scope of ITAR

- The ITAR is administered by DDTC
- Four categories of articles that require license or approval:
  - Defense articles on the USML
  - Activities of persons that qualify as “brokering” activities
  - Information that is considered “technical data.”
  - Services that are considered “defense services”
- Not just exports – companies must be registered with DDTC if they manufacture, broker or export defense articles or services
What is a Defense Article?

“Defense Article” is an article that is:

- Specifically designed, developed, configured, adapted or modified for military application
- Does not have predominant civil application
- Does not have performance equivalent to items with civil application

OR

- Has “significant military or intelligence applicability” such that control under ITAR is necessary

- The intended end use of the item does not govern
- DDTC has significant discretion
The USML

- A list of the articles, technical data and services covered by ITAR
- This list covers items that are specifically designed for military application, and lack a “predominant civil application”
- A license from DDTC is generally required to export, reexport or transfer defense articles or services covered by the USML
What is Technical Data?

- ITAR controls “technical data”
- Technical Data is:
  - Information required for the design, development, production, manufacture, assembly, operation, repair, testing, maintenance, manufacturing or modification of defense articles
    - Includes information in the form of blueprints, drawings, photographs, plans, instructions or other documentation.
  - Classified Information
  - Information covered by invention secrecy order
  - Software
What are Defense Services?

- Furnishing assistance (including training) to foreign persons
  - Whether in the United States or abroad
  - Covers design, development, engineering, manufacture, production, assembly, testing, repair, modification, operation, demilitarization, destruction, processing, installation, integration, training, or use of defense articles
- Furnishing controlled technical data to foreign persons
- A defense service may be performed:
  - regardless of whether the underlying defense article is of U.S. or foreign origin,
  - even when no controlled “technical data” is involved
Exports Under ITAR

- Sending or taking a defense item, including technical data, out of the United States in any manner
- Transferring registration, control or ownership to a foreign person of any aircraft, vessel, or satellite covered by the USML, whether in the United States or abroad
- Disclosing (e.g., oral or visual) or transferring
  - in the US any defense item to an embassy, any agency or subdivision of a foreign government (e.g., diplomatic missions)
  - technical data to a foreign person wherever located
  - A foreign person is an individual or entity who is not a U.S. citizen, permanent resident, or person granted refugee or asylum status
- Performing a defense service on behalf of, or for the benefit of, a foreign person, whether in the United States or abroad
“Broker” under ITAR means any person who engages in “brokering activities”

“Brokering activities” includes the financing, transportation, freight forwarding, or taking any other action that facilitates the manufacture, export or import of a defense article or defense service

Brokers must register, except for persons exclusively in the business of financing, transporting, or freight forwarding . . . Air carriers and freight forwarders who merely transport or arrange transportation for USML items are not required to register - 22 CFR 129.3

In fact, DDTC will not accept registration applications from forwarders
ITAR and Freight Forwarders

- Licensees responsible for acts of agents to whom defense articles are entrusted, including for transportation
- Forwarders for licensed goods are identified and authorized in the license
- Licenses (with supporting documentation) for export of hardware must be deposited with CBP prior to export and prior to AES filing
- Must file export information via AES—8 hours pre-departure for air and truck; 24 hours pre-departure for rail and sea
Example Prohibitions of ITAR

- Under the ITAR it is Unlawful to:
  - Export (or import), attempt or conspire to export, or cause, or aid or abet or permit to be exported a defense article or technical data without first obtaining a license (unless exempt)
  - Use any export document containing a false statement or misrepresenting a material fact for the purpose of exporting any defense article or technical data or furnish any defense service
  - Participate in transaction in which debarred or ineligible person may have direct or indirect interest
  - Violate any of the terms and conditions of a license
Overview of Census Foreign Trade Regulations
Census Regulations Overview

- Mandatory AES and proof of filing annotation requirements
- Responsibility of Parties, including in routed transactions
- Correcting EEI, Penalties and Voluntary Disclosure
Mandatory AES and Annotations

- Electronic Export Information (EEI) must be filed electronically via AES
- Filers must be certified to file by AES
- For most items the proof of filing citation or exemption legend must be noted on the first page of the B/L or AWB
- Agent (forwarder) or USPPI must provide this to carrier and carrier uses it to make same annotations to outbound manifest
Responsibilities of Parties (Ordinary Export Transaction)

- Ordinary Export Transaction (Forwarder is AES Filer)
  - USPPI
    - Provide agent with POA,
    - Provide agent accurate and complete information on goods and export transaction
    - Retain records
  - Agent (i.e., Forwarder)
    - File complete and accurate information
    - File timely
    - Respond to AES messages, i.e., errors and alerts
    - Provide proof of filing citation or exemption legend to carrier
    - Promptly file corrections to EEI
    - Retain records
Responsibilities of Parties (Routed Export Transaction)

- Routed Export Transactions
  - FPPI
    - Issue POA to US agent authorizing facilitation of export
  - USPPI
    - Provide name, address and EIN to agent
    - Provide description of goods, quantity, value and origin
    - Provide HTSUS or Schedule B numbers
    - Provide ECCN or sufficient technical detail to allow export classification
    - Licensing information (*but see* routed transactions under EAR)
  - Agent (*i.e.*, Forwarder)
    - Obtain POA from FPPI (and provide copy to USPPI upon request)
    - File timely
    - Respond to AES messages, *i.e.*, errors and alerts
    - Provide proof of filing citation or exemption legend to carrier
    - Promptly file corrections to EEI
    - Retain records
Corrections, Penalties, Disclosures

- Civil penalties of $10,000 per violation for violations of Census FTR, including failure to file, late filing, filing incorrect information, failure to make required annotations
- Automated nature of AES leading to increased enforcement of all export laws
- Census has adopted a voluntary self-disclosure provision in its regulations
- Disclosure strongly encouraged and is mitigating factor in penalty determinations
- Consider impact of mandatory correction of EEI requirements (15 CFR 30.9)
Export Compliance Concepts for Transportation Providers

- General Approach
  - Senior Management Commitment
  - Formal written compliance policy and program
  - Organization and designation of responsible personnel
  - Training
  - Internal audits
  - Published method for employee reporting of violations
  - Strong Recordkeeping Program
Export Compliance Concepts for Transportation Providers

- Screen all parties to transactions, including:
  - Sold-to
  - Ship-to
  - Distributor
  - Notify party
  - In-transit/intermediate consignee
  - End-user
  - Freight forwarder
  - Bank
  - Other?

- Screening can be manual, but automated solutions abound

- Develop “Know Your Customer” procedures, including attention to red flags
**Export Compliance Concepts for Transportation Providers**

- Consider instituting special processes for shipments to certain destinations, *i.e.*, known transshipment hubs, such as Dubai, Malaysia, Singapore.
- If part of a global network or global company, address compliance policies appropriately with foreign partners.
- Develop strict policy about and carry out careful vetting before acting as agent in routed export transaction, especially under EAR.
- Develop special security and handling procedures for specific customers, *i.e.*, ITAR customers.
- Address compliance responsibilities in contracts and in writing.
Q & A

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