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Export Controls and Policy Update

A recent three-day conference on *Export Controls in Transition* sponsored by the U.S. Department of Commerce confirmed the Obama Administration's commitment to reform of U.S. controls on exports. Both President Obama and Secretary of Commerce Gary Locke addressed the conference, demonstrating support for reform at the highest levels. The president, the secretary and other officials also emphasized, however, the administration's commitment to export control enforcement, both during the current transition period, and after reforms are implemented.

Reform Goals

At present, the Departments of the Treasury (Office of Foreign Assets Control) ("OFAC"), Commerce (Bureau of Industry and Security) ("BIS"), State (Directorate of Defense Trade Controls) ("DDTC") and Defense (Defense Technology Security Administration) all have major roles in export controls and licensing. There are two major lists of controlled goods and technology. BIS maintains the Commerce Control List ("CCL"), which regulates exports of "dual-use" items, that is, items and related technology that have both commercial and military or other strategic uses against U.S. national interests, such as terrorism or nuclear proliferation. DDTC maintains the U.S. Munitions List

("USML"), which regulates exports of defense items and related technology. Determining which list applies to a given export is not always clear, the control policies underlying the lists are not always consistent, the licensing procedures differ from agency to agency, and the agencies use incompatible computer systems. OFAC maintains yet a third export control regime, aimed at transactions with specific embargoed countries and persons. Because its controls can apply to all exports to a sanctioned destination, OFAC does not maintain a list of banned goods or technology, but does maintain a list of Specially Designated Nationals with which US entities are not to do business. There are also various other lists of proscribed persons and entities maintained by other agencies. As President Obama stated in his address to the conference, "the current export control system is overly complicated, contains too many redundancies, and, in trying to protect too much, diminishes our ability to focus our efforts on the most critical national security priorities."

The reforms would initially seek to align the CCL and USML into consistent lists, divided into three tiers. Applying a principle of "higher fences around fewer items," a license would generally be required for all items in the highest tier to all destinations, and in a number of instances export approval may be

denied. Most if not all items in the second tier could be exported under a license or licensing exemption to our trusted trading partners and allies. Items in the third tier would generally not require a license. Industry input may help determine the scope of the tiers. In addition, the reforms contemplate making the control lists largely positive rather than negative. That is, the lists would specifically identify the types of goods or technology that are controlled, rather than controlling everything in a particular category unless it is specifically exempted. Ultimately, alignment of the lists through organization into three tiers and the use of positive controls should facilitate consolidation of the two lists into one.

In addition, the administration intends to establish an Export Enforcement Coordination Center (“EECC”), to coordinate and strengthen export controls enforcement and eliminate gaps and duplications across all relevant departments and agencies. The ultimate goal would be for this EECC to become the single export control agency, although this and the consolidation of the control lists may require legislation and thus significant additional time and effort.

The overall result of the reforms should be a less restrictive set of export controls, making necessary controls more effective and the licensing process more efficient. These reforms should also facilitate coordination with our trusted trading partners and allies on multilateral controls.

Export Compliance

In furtherance of the reform, there have been some initial efforts to conform the USML and the CCL in certain limited

areas, and there have been significant changes in the control of encryption technology by BIS. Otherwise, the existing multi-jurisdictional control regime remains largely in place, with officials from all the relevant agencies expressing their continuing dedication to rigorous enforcement of the existing controls unless and until they are changed. Some points of particular interest from the various panels at the conference included:

- Cloud computing. Using a cloud computing service to store data or other information relating to the development, production or use of CCL items could involve an export of controlled technology if the “cloud” includes servers in a controlled destination (such as, for certain purposes, India and China).
- Deemed exports. A “deemed” export occurs if controlled information or technology is disclosed to a national of a controlled destination, even if the transfer occurs in the U.S. Because the transaction occurs in the U.S., it may not be recognized as a controllable export.
- Re-exports. A re-export occurs if controlled items or technology are sent to an authorized destination or end-user, and then diverted from there to a destination or end-user for which authorization has not been obtained. From an enforcement perspective, the end result is the same as if the controlled items or technology were sent directly to a controlled destination.

- “Destinations of Diversion Concern.” Under the new stricter controls on trade with Iran mandated by the Comprehensive Iran Sanctions, Accountability, and Divestment Act of 2010, which went into effect in July, the president is authorized to designate countries as not making sufficient efforts to control diversion of certain materials to Iran. Licenses for exports of those materials to these “Destinations of Diversion Concern” would be subject to a presumption of denial.
- Diversions generally. A move to “higher fences around fewer items” is likely to heighten concerns about possible diversion of authorized exports to unauthorized destinations or end-users. As a consequence, it is likely that there will be a greater emphasis on policing end-users and end uses of exports, in order to prevent diversion of controlled goods and technology to proscribed destinations or users.
- Re-exports and other diversion concerns underscore the need for appropriate due diligence on the *bona fides* of proposed end-users and end uses for potentially controlled exports.
- Increased cooperation among enforcement agencies. A number of recent settlements of cases involving export violations, some featuring settlements substantially above \$100 million, have been the result of joint efforts by two or more of the above agencies, and in some cases the Department of Justice as well (for example

in cases involving allegations of criminal violations). There was general support among enforcement officials for further cooperation in investigations and prosecutions.

→ Corporate compliance programs can be an important factor in mitigation of penalties.

→ The prohibitions against participation by US persons or entities in the Arab boycott of Israel, and against bribery of officials of foreign governments or political parties under the Foreign Corrupt Practices Act, remain areas for active enforcement.

In summary, consistent with its goal of increasing U.S. exports, the administration is moving toward a more rational and efficient export control regime, but controls will remain a fact of life for exporters for the foreseeable future.

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